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# **PROJECT 1p/05 – 3**

## **Application of the PPP Principle on the Economic and Social Cohesion Policy**

Final Report  
for the Ministry for Regional Development  
of the Czech Republic

May 2006

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# 1 Executive Summary

## 1.1 Project Methodology

### Contents of the document

This document summarizes results of Project 1p/05-3 “Application of the PPP Principle on the Economic and Social Cohesion Policy” (hereinafter the “Project”) whose focus was based on the tender dossier of the Community Support Framework Department of the Ministry for Regional Development and on the on-going discussions with and recommendations of the staff of the CSF Department and other state authorities involved. The report is based on information acquired during the first three months of 2006 and it was drafted by a consortium composed of representatives of Deloitte, Elbona, CopiRisco and the Havel & Holásek law firm.

### Goal of the project

The goal of the project is to identify possible combinations of PPP projects and financing under the Funds and following the identification of options to compile a list of recommendations for programming and preparation for implementation during the programming period (2007-2013).

### Project objectives

- Analyse legal documents on the EC level and on the level of the Czech legal framework governing PPP projects;
- Identify barriers of combining PPP projects and co-financing under the Funds;
- Define specific recommendations to eliminate the impact of barriers;
- Identify suitable areas for PPP projects implementation;
- Define basic models combining PPP projects and the Funds;
- Develop a model project.

### Document structure

The project is divided into two main parts by its topical focus. The first part of the document deals with an analysis of the Community law and the legislation of the Czech Republic in relation to PPP projects. The second part of the document identifies relevant barriers and risks which may have a negative impact on the possible implementation of PPP projects co-financed under the Funds. For the sake of transparency, the barriers and risks are structured into two main levels:

1. Programme-related – barriers and risks at this level may serve as a basis for discussion with the European Commission and the Czech Government, and possibly also with relevant ministries and managing authorities.
2. Project-related – issues of this level may be discussed at the level of individual managing authorities when preparing operational programmes and manuals for beneficiaries.

Also, the analysis classifies the barriers and risks to the following sub-sections: legal, barriers related to the financing structure, organizational and procedural barriers and others. There is a brief description of each barrier, including its potential risk. The first draft list of barriers was discussed individually with the staff of the ministries and other involved entities catering for the Funds and PPP projects (a list of meetings is provided in Annex No. 5) and also discussed at a workshop on Project Phase I held on 22 February, 2005. Conclusions of the workshop indicated that ministries were very much interested in setting models for implementation of PPP projects co-financed under the Funds in

terms of defining the role of the beneficiary, infrastructure owner or another subject matter of the investment and in terms of defining contractual terms and conditions between the public body and the operator. The second priority area was the cash flow and applying the financial gap calculation in compliance with Fiche No. 64 to particular project cases. Therefore, a special chapter 5 “Basic Models Combining PPP and EU Funding” is dedicated to these two issues. The issue of financing is described in chapter 8.6.1 “Calculation of the EU Contribution to the Jihlava CAMPUS Project”.

The project team strived to be flexible, to respond to the current development and to include as many as possible prerequisites and requirements arising from statutory instruments and fiches published during the project implementation.

When working on chapter 4 “Areas Proposed for Combining PPP and EU Funding by Individual Operational Programmes”, current draft priorities of OPs provided as at 17 March, 2006 were used as a basis. The issue of implementation of projects based on the PPP model was discussed in detail with the authors of particular OPs and conclusions of these meetings suggested which state authorities were interested in their implementation. Certain OPs also identify specific projects, however the list is not complete due to the absorption capacity mapping which is currently underway. Outputs of the absorption capacity mapping were not available before the end of this project implementation. Chapter 6 “Technical Assistance” contains comments on the current description and proposed form of use of technical assistance funding for relevant OPs and also further activities which we believe are characteristic for financing under the aforementioned Funds. There are plans to conduct a technical seminar with the Commission to discuss key problematic areas of combining PPP projects co-financed under the Funds. Next chapter 7 gives a basic characteristic of a PPP project and further gives specific features of PPP projects which must be reflected in selected chapters of the operational programmes/instructions to beneficiaries. It is a general text which we believe can be universally applied to all OPs considering use of PPP projects. Last chapter 9 “Recommendations” presents main topics we recommend to resolve with respect to creation of favourable conditions for implementation of PPP projects co-financed under the Funds. The structure of recommendations corresponds with identified barriers and there is also information on the type of barrier/risk – programme-related, project-related with impact on the Czech Republic or the EU – on which level an effective solution could be reached – the European Commission, Government, ministries and/or managing authorities. As mentioned in the legal analysis, the European Commission has no comprehensive instrument dealing with PPP projects and it is necessary to avoid potential risks and to clarify them before PPP projects are implemented, in order to avoid additional reduction of the co-financing rate and to avoid undesirable time delays during the project implementation phase.

## Restrictions

The main restriction of project activities with respect to the set prerequisites was the fact that the OPs were still being in the process of drafting and suitable priorities for PPP projects could not be clearly selected as we did not have information on the financial allocations per priorities, maximum contributions from the Funds per project, and an overview of supported activities. In this respect, we appreciate pro-active approach of the Ministry for Regional Development when acquiring requested information from individual authors of the OPs.

## 1.2 Findings and recommendations

### Major Barriers and Risks

#### Barriers and risks at the program-level linked to the European Commission:

- Eligible expenditures must be paid in full amount by the beneficiary; (barrier)

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- on-going use of subsidies<sup>1</sup> from EU<sup>2</sup> funds during the project investment phase contradicts the key PPP principle: “no service, no payment“; (risk)
- automatic classification of all PPP projects as the project group generating income (including the projects based on fees for availability); (risk)
- investment costs in the operational phase cannot be financed from EU funds. (barrier)

### **Barriers and risks at the program-level linked to the Czech Government, ministries and managing authorities:**

- Impact of state aid rules on individual PPP projects; (barrier)<sup>3</sup>
- infrastructure owned by the private sector; (barrier)
- to-date, PPP project-specific costs (incurred mainly during the preparation phase) cannot be financed from EU funds; (risk)
- insufficient standardisation of PPP project-related documentation (tender documentation, concession contracts). (risk)

### **Barriers and risks at the project-level:**

- Different interpretation and routine application of the Public Procurement Act; (risk)
- risk of changed concession contract terms during the use of subsidy under EU funds by a given PPP project – due to the missing standardisation of some concession contract provisions required for combined EU and PPP funding; (risk)
- for the public sector, combined PPP and EU funding is demanding in terms of time, administration and costs; (risk/barrier)
- relatively complicated cash flow of a PPP projects co-financed from EU funds; (risk)
- to prepare a detailed list of eligible PPP projects, absorption capacity thereof should be mapped within relevant operational programmes. (risk)

### **Sector-Specific Projects**

- Combined PPP and EU funding seems to be most efficient if used on large infrastructure projects in the transport sector and in the environmental field (investment costs > CZK 1 billion).
- Although operational programmes in transport, environment, business and innovation, and competitiveness seem to be the most desirable for a combined PPP and EU funding under current conditions, this type of funding may also be effective in other OPs, if there are convenient projects.
- Regional operational programmes represent a separate category – implementation of several large projects is, in theory, possible.

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<sup>1</sup> On-going use means a submission of request for payment during the project implementation, after each phase is completed.

<sup>2</sup> EU funds mean Structural funds and Cohesion Fund.

<sup>3</sup> The issue is a difference between PPP project rules and the policy on Economic and Social Cohesion. On PPP projects, infrastructure is owned, as a rule, by a private investor while the policy on Economic and Social Cohesion imposes the beneficiary as the owner of infrastructure. This fact must be taken account of and the concession contract drafted accordingly, as a contract of lease.

## PPP and EU Funding Models

Model 3 – “Public Beneficiary Model” is considered the most convenient model out of the models mentioned in Chapter 5 (see chapter 5.2.1). However, the selection of the most convenient model depends, to a great extent, on the project itself.

Advantages:

- The maximum subsidy from EU funds for PPP projects up to the limit of 85 percent of eligible costs of the financial gap;
- financing of investment costs by a private entity (granting of a non-interest-bearing loan or commercial loan);
- using the advantages of the DBFO model (DBFO model = Design-Build-Finance-Operate);
- motivation of the private entity for minimum overall project costs and performing all supplier services;
- lower operational costs of the project (the private operator may influence the project design); and
- greater chances of transferring risks to the private entity.

Disadvantages:

- Need to deal with the issue of paying investment costs by the beneficiary; and
- under the current conditions, the structure of clearing the project costs is rather difficult because the operator (SPV) cannot pay the invoices directly to the supplier but needs to grant a non-interest-bearing loan to the beneficiary who pays supplier invoices.

## Key Recommendations

### Key recommendations at the program-level with relation to the EC:

To allow for an effective combination of PPP and EU funds in the programming period, we consider it useful to initiate technical consultations with the EC aimed at clarifying the interpretation of the following points:

- Eligible costs will be covered by the private entity during project implementation; invoices will be enclosed in the application for payment; the public entity will pay its liabilities during the programming period in the form of service fees;
- payment of the investment costs of the project in the operational phase (the “infrastructure component”);
- projects based on the payment of shadow toll and infrastructure/service availability fees paid by a public entity to a private partner should not be automatically included among income-generating projects;
- infrastructure owned by a private applicant during the operational phase provided that the project purpose does not change over the period of sustainability of the project; and
- the question of determining the acceptable level of profitability of projects (based on the indicative income percentage defined for selected fields in Fiche 64; and based on what grounds is it justified to exceed this percentage in individual projects).

### Key recommendations at the program-level with relation to the government, ministries and managing authorities:

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- Large infrastructural projects especially in transport and environment (investment costs > CZK 1 billion) seem to be best suited for effective combination of PPP and EU funds;
- define consistently the understanding of PPP projects at the level of all resorts and set up a standard approach to the preparation and follow-up implementation of PPP projects;
- realistically assess the opportunities of individual operational programmes and subsequently select PPP projects eligible for co-financing through a specific operational program;
- perform a detailed selection of PPP projects on the shortest possible time horizon;
- prepare an indicative list of potential PPP projects combined with EU funds in the Czech Republic (according to individual operational programmes) at the level of managing authorities;
- standardise documentation related to PPP projects (tender documentation, concession contracts – standard provisions relating to EU funds);
- deposit funds provided from EU funds to the blocked account of the private entity (operator) to be drawn on condition that the private entity duly meets its contractual conditions;
- include costs associated with project documentation of PPP projects in the operational programme, or, for selected projects, to technical assistance priority; and
- strengthen capacities at the level of managing authorities.

### **Key recommendations at the project-level with relation to managing authorities:**

- Explore opportunities to use EU funds for each contemplated PPP project;
- begin preparation of combined projects well in advance;
- prepare projects with the assistance of specialised advisors;
- prepare a detailed feasibility study of the project before submitting the project application;
- invite tenders for licensees before registering the application for an EU funded project;
- select of the most convenient PPP model and the type of beneficiary (public or private entity) for each project. The main aim is to ensure the maximum subsidy from EU funds for PPP projects based on the results of the financial analysis calculated for both scenarios where the grant either amounts to 85 percent of the financial gap calculated from eligible expenditure or the grant amounts to 40 percent of eligible expenditure;
- assess issues related to the ownership structure always with respect to a specific project;
- define, in the concession contract, information requirements and the impact of major changes in PPP terms and conditions on financing – the objective is to ensure claims, if any, for returning the subsidy from EU funds; and
- define control and monitoring conditions during project implementation in the concession contract.

### **Conclusion**

The foregoing analysis indicates that PPP projects may be combined with EU funds. However, the structure for such initiatives is rather complicated and thus the implementation of PPP projects needs to focus on:

- Selected areas (such as transport infrastructure, environment, brownfields);
- large-scale projects whose volume is at least CZK 1 billion;
- project plans whose implementation may start within three years.

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Some issues require clarification at the level of the European Commission, especially issues associated with the financing system (for example, the payment of eligible expenses of the project by an entity other than the beneficiary; from the perspective of the beneficiary, these expenses will represent contingent liabilities not paid until the operational phase of the project).

## 2 Analysis of Selected European Documents in relation to PPP and Czech Legal Environment

As at today, there are no comprehensive arrangements for PPP projects in the Community law. However, relevant regulations and statutory instruments for the ESC mention in some of their provisions also implementation of PPP projects co-financed under the Funds. However, it is a mere statement about the existence of such a possibility without any detailed specification of conditions and procedures.

The aim of this legal analysis is to assess to which extent the rules of ESC could be applied to PPP projects. There will be measures proposed for the identified barriers, that is how to avoid them effectively without jeopardizing drawing on the Funds.

### 2.1 Regulations on the Structural Funds and the Cohesion Fund

So far, the legislative form of the regulations governing the Funds for the future programming period (2007-2013) has not been finalized. One may assume that changes, if any, will be only insignificant and they should not affect the ESC rules, the programming system, building and composition of the implementation structures and standardized procedural mechanisms related to the drawing on the Funds.

This study is based mainly on the Council Regulation laying down general provisions on the ERDF, the ESF and the Cohesion Fund (hereinafter the “General Regulation”) and draft regulations on each of the Funds and the statutory instrument on the General Regulation.

In the explanatory memorandum to the General Regulation, the Commission insists on maintaining the ESC principles – programming, partnership, co-financing and evaluation. The reforms outlined in the draft regulations should cover the following areas (the reforms also touch upon the PPP issue):

- supporting a more strategic approach to programming;
- further devolution of powers within the framework of existing partnerships in Member States;
- fostering more transparent partnerships and stricter control mechanisms;
- simplification of the managing system by introducing more transparency, differentiation and proportionality and at the same time providing for sound financial management.

#### 2.1.1 PPP in the Process of Programming and Management

##### 2.1.1.1 ESC Principles

Primarily, there are two principles of the ESC policy impacting the public-private partnership: additionality<sup>4</sup> and the only one fund approach.

##### Additionality

The additionality principle lies in complementing, not replacing, national financing by the Funds. However, in compliance with the proportionality principle, the Commission limits its control only to

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<sup>4</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 13(1)

the “Convergence” objective. For the remaining two objectives, observance of the additionality principle shall fall within the responsibility of Member States.<sup>5</sup> The Commission shall, in co-operation with the Member State, verify additionality in 2011 and ex-post by 31 December, 2016 for the “Convergence” objective.

For regions covered by the “Convergence” objective, there must be determined the level of public or equivalent structural expenditure which the Member State shall maintain during the whole programming period.<sup>6</sup>

#### Only one fund principle

The second out of mentioned principles is the only one fund principle, i.e. operational programmes may only receive financing from only one EU fund (the ERDF or the ESF), with the exception of OP Transport and OP Environment where support may be provided jointly from the ERDF and the CF.<sup>7</sup>

The only one fund principle is partially affected by the rule of cross financing allowing for each priority of the OP to finance measures falling within the scope of assistance to the other fund (such as to support training from the ERDF), provided that they are necessary.<sup>8</sup> The amount of such financing may reach up to 10% of the financial allocation for a given priority.

When considering PPP project financing under the Funds, it is important to take this principle into account, in particular due to the complexity of PPP projects which by their nature and composition of expenditure may involve more than one fund.

#### 2.1.1.2 Financial Management, Control and Monitoring

Within the monitoring framework, Member States shall carry out ex-ante and interim evaluation of OPs based on which implementation mechanisms of the OPs may be adjusted. The responsibility of the Commission is based on the ex-post evaluation of OPs per objectives.<sup>9</sup>

Within the OP management, each Member State shall ensure that all the control mechanisms of management, such as an internal audit, monitoring of irregularities, financial reporting systems, etc. are in place. Also, it shall establish an audit authority responsible for verification of the effective operation of the management and control system and a monitoring committee for each OP responsible for monitoring of activities of the managing authority and other tasks related to the OP implementation.<sup>10</sup>

The guarantee of the legality and regularity of expenditure declared is based on the results of national controls. Based on this fact, the Commission will be able to restrict its on-the-spot checks only to exceptional circumstances. Similarly, the level of the Commission intervention in the administration, evaluation and control will depend on the significance of its contribution. Thus, Member States will be able to use their own rules and structures of administration and management where the national contribution significantly prevails.<sup>11</sup>

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<sup>5</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 13(4)

<sup>6</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 13(2)

<sup>7</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Articles 33(1) and (3)

<sup>8</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 33(2)

<sup>9</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Articles 62-67

<sup>10</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Articles 61-62

<sup>11</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Articles 71-72

The system of financial management, monitoring and control in the new programming period lays down the rules for the PPP projects which must form an integral part of the concession agreement. Failure to comply with these rules may result in repayment of a part or the whole contribution to the EU budget.

### 2.1.1.3 Project Preparation

Due to its complexity, preparation of PPP projects requires substantial means and funds; however, new regulations do not specifically describe these activities. Nevertheless, we recommend financing model projects from funds allocated to the technical assistance (see 6.2.).<sup>12</sup> The expenditure for the preparatory phase of a project, in particular, for the preparation of project documentation is considered to be eligible expenditure and therefore it could be financed directly from the financial allocation of the relevant OP priority. In such a case, it can be expected that eligible expenditure for the preparation of the project documentation will have a percentage ceiling. For major projects (see 2.1.1.4) there will also be free-of-charge counselling services provided for preparation of project documentation within new initiatives of the Commission and the EIB (see 2.1.1.5).

### 2.1.1.4 Major Projects and PPP

Should the costs of contemplated PPP projects exceed EUR 25M in the case of the environment and EUR 50M in other fields, they may be classified as major projects and they may be explicitly listed in the OPs.<sup>13</sup> Major projects are submitted for assessment to the Commission and the following information set forth in Article 36 of the General Regulation must be stated:

- information on the body to be responsible for implementation;
- information on the nature of the investment and a description of it, its financial volume and location;
- the results of the feasibility studies;
- a timetable for implementing the project (and, where the implementation period for the operation concerned is expected to be longer than the programming period, the phases for which Community co-financing is requested during the 2007-2013 programming period);
- a cost-benefit analysis, including a risk assessment and the foreseeable impact on the sector concerned and on the socio-economic situation of the Member State (and/or the region and, when possible, of the other regions of the Community);
- environmental impact assessment;
- a justification for the public contribution;
- the financing plan showing the total planned financial resources and the planned contribution from the Funds, the EIB, the EIF and all other sources of Community financing, including the annual schedule of the financial contributions from the ERDF or the CF.

The time schedule of preparation of programming documents for 2007-2013 indicates that the required data must be available before May 2006 so that they could become a part of the OP structure.

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<sup>12</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 43(1)(a)

<sup>13</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 38

#### 2.1.1.5 New Initiatives of the Commission and the EIB

The most suitable procedure for preparation of PPP projects we recommend for consideration is a possibility to consult potential projects with the European Investment Bank and the European Investment Fund. The Commission explicitly invites Member States to involve the EIB and the EIF to the programming, financing and preparation of major projects in particular and to establish public-private partnerships.<sup>14</sup>

The assistance of the EIB and the EIF in the new programming period is directed through three new initiatives:

- JASPERS<sup>15</sup> (Joint Assistance in Supporting Projects in European Regions) – provision of counselling services for the preparation of major projects, in particular in the field of transport and the environment;
- JESSICA (Joint European Support for Sustainable Investment in City Areas) – support of sustainable investment, growth and jobs in urban areas;
- JEREMIE (Joint European Resources for Micro to Medium Enterprises) – improving access to financing for development of micro, small and medium enterprises in the EU regions.

In the case of JEREMIE, the mutual fund will announce calls for financial intermediaries that will then provide financing to micro-, small- and medium-sized enterprises for specific projects.<sup>16</sup> The assistance under JEREMIE initiative is composed of two phases: In the first phase (2006-2007) current financial instruments in Member States and regions will be assessed and potential needs will be outlined. In the second phase, managing authorities will release financing from OPs to special-purpose venture capital funds, guarantee and loan funds (the so-called financial engineering measures), or to mutual funds which are to serve as an intermediate step between OPs and financial engineering instruments. Mutual funds will be used in the cases of investing to multiple financial engineering measures and should this method be more appropriate from the administrative viewpoint.<sup>17</sup> Release of financing to mutual funds will be done in the form of interim payments from the ERDF.<sup>18</sup> In this case the use of PPP projects is restricted by types of projects and beneficiaries.

In the case of JESSICA, it is a direct and unequivocally declared support to public-private partnership and projects within city areas. Financial support will flow to beneficiaries without the intermediate step of mutual funds, i.e. by direct transfer of financing of the OPs to a special urban development fund and then to beneficiaries.<sup>19</sup>

Financial support via JASPERS has a structure based on consultations with experts of the EIB and the European Bank for Reconstruction and Development (EBRD) which is voluntary and is not conditioned by drawing on loans from these institutions. Similarly, neither the EIB nor the EBRD will be obliged to grant any loans or privileges with respect to the consulted projects.

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<sup>14</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 35(2)

<sup>15</sup> Jaspers is an initiative of the Commission, the European Investment Bank and the European Bank for Reconstruction and Development covering areas under the Convergence objective. Supported priority areas and objectives will be identified in the Action Plan to be drafted for each year; first projects will be selected in the first quarter of 2006.

<sup>16</sup> Fiche No. 60

<sup>17</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 42

<sup>18</sup> Fiche No. 60

<sup>19</sup> Fiche No. 61

## 2.1.2 Contributions from the Funds

### 2.1.2.1 Factors Determining the National Co-financing Rate

The regulation sets forth ceilings depending on the average GDP per capita in 2001-2003 when compared to the EU-25 average. Based on the average GDP per capita the Czech Republic is divided to the “Convergence” objective (all regions with the exception of Prague) and the “Regional competitiveness and employment” objective (Prague). The Czech Republic did not reach 85% of the EU-25 average<sup>20</sup> and thus receives contribution in the maximum amount of 85% from the Funds within the Regional competitiveness and employment objective and the Convergence objective. The same ceiling applies to the CF (applies also to Prague).<sup>21</sup>

The maximum co-financing rate under the Funds is defined on the level of programmes, not on the level of priorities. The contribution rates are also impacted by other factors listed in Article 50(a)-(f) of the General Regulation. One of these factors mentions mobilisation of private financing, in particular under public-private partnerships.<sup>22</sup>

Another factor impacting the co-financing rate under the Funds is the type of the beneficiary, if it is a public entity or a private entity<sup>23</sup>. For private entities, the contribution must comply with the state aid rules. For the Czech Republic, the permitted level of aid is laid down in the Regional Map of State Aid Intensity which is currently being processed for the new programming period (2007-2013). Available information indicates that the amount of state aid for commercial entities reaches the limit of 40% in all regions with the exception of Prague (state aid for Prague is up to 15%) and the South-West cohesion region (state aid up to 36% for 2007-2010 and 30% for 2011-2013).

### 2.1.2.2 Restriction of Co-financing Rate for Revenue-Generating Projects

Article 54 of the General Regulation governs financing of revenue-generating projects under the Funds. This is especially important for PPP projects as almost all PPP projects directly depend on the revenues from the user or the public sector. The context of this provision indicates that revenue-generation means any operation including investment in infrastructure the use of which involves fees borne directly by users and any operation resulting from the sale or rent of land or buildings or any service provided for consideration.<sup>24</sup>

In the case of such projects, eligible expenditure shall be calculated on the basis of the investment cost less the current value of the net revenue from the investment over a specific reference period.<sup>25</sup>

The amount of contribution under the Funds is calculated using a financial gap method (in some cases the term “financing deficit” is used). The financial gap equals the difference between discounted investment cost and discounted net revenue of the project (the amount of discounted cost not covered by discounted revenue).

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<sup>20</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Annex II

<sup>21</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 51(1)-(3) and Annex 2

<sup>22</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 50(d)

<sup>23</sup> Both the public entity and private entity can meet the attributes of state aid, dependent on their services. For simplification, hereinafter will be used the term “private entity instead” of “undertaking”; the entity which does not meet the conditions of an undertaking will be called a “public entity”.

<sup>24</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 54(1)

<sup>25</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 54(2)

The financial gap, however, does not determine the contribution level from the Funds. Therefore, out of the total investment cost eligible part must be identified complying with the rules of the Funds and thus the level of financial gap must be adjusted. Then, based on ceilings set for individual priorities, the maximum contributions from the Funds will be determined.

Determination of the contribution:<sup>26</sup>

Step 1: calculation of the financial gap

$$R = \frac{\text{Max EE}}{\text{DIC}} = \frac{\text{DIC} - \text{DNR}}{\text{DIC}}$$

R – rate of financial gap

Max EE – maximum eligible expenditure

DIC – discounted investment cost

DNR – discounted net revenue, calculated as discounted revenues less discounted operating costs + discounted residual value

Step 2: calculation of the co-financing rate for a specific priority

$$DA = EC * R$$

DA – co-financing rate for a specific priority

EC – eligible cost

Step 3: calculating the maximum grant amount

$$\text{EU grant} = DA * \text{Max CRpa}$$

EU grant – grant under the Funds

Max CRpa – maximum co-financing rate fixed for the priority axis

### Other factors impacting calculation of the financial gap

For the calculation, the managing authority takes into account the reference period adequate for the category of the relevant investment. The calculation of the financial gap for revenue-generating projects and then the amount of contribution from the Funds are impacted also by other factors, such as profitability normally expected of the category of investment concerned, of the application of the polluter-pays principle, as well as of the principle of equity linked to the relative prosperity of the Member State concerned.

#### a) Normally expected profitability<sup>27</sup>

Expected profitability of investment is expressed by the internal rate of return (IRR) representing a discount rate at which the net present value equals zero (difference between discounted revenue and discounted investment cost).

<sup>26</sup> Fiche No. 64

<sup>27</sup> Fiche No. 64

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Therefore, Member States are required to identify a suitable discount rate which will determine reasonable profitability of investment. The rate depends on the risk level and circumstances such as socio-economic context of the country/region, problems with the project implementation, economic life cycle of the project, currency risk and mainly risk related to the estimated project revenue.

Based on the experience gained so far, there are indicative internal rates of return determined expressing the expected profitability of the project:

- power industry 7.0%
- water management and environment -0.1%
- transport 6.5%
- other services 4.2%

### b) Polluter-pays principle

This principle concerns projects financed under the ERDF and the CF where the environmental polluter must bear the costs related to generation of negative externalities. These contributions may be included into the project revenue and the contribution from the Funds per project may be adjusted.

### c) Availability from the viewpoint of revenue

Availability from the viewpoint of revenue in the Member State concerned, in other words the principle of equity linked to the relative prosperity when defining contributions from the Funds for projects taking into account the wealth of the Member State or region concerned should also be taken into account when making an economic analysis of revenue-generating projects. In practice it means that the lower the regional (national) revenue, the higher the expected contribution from the Funds.

### Relation of revenue-generating projects and PPP

PPP projects are characterised by the fact that part of the risk of their implementation is transferred to a private sector partner. This “risk transfer” can be expressed in the financial analysis by increasing a discount rate. An average discount rate is 5%<sup>28</sup> and Member States are recommended to use consistent rates for similar projects in the same region/country, and therefore the rates should form part of their methodology documents. In the case of PPP it is appropriate to calculate economic indicators with a discount rate above this level.

A specific feature which may impact the calculation of economic indicators of PPP projects is additional revenue not included in the initial calculation. Should it be discovered within three years after closing an OP that a particular operation generated revenues not taken into account in the calculation of the financial gap, such revenue must be repaid to the EU budget in proportion to the contribution from the Funds.

#### 2.1.2.3 Eligibility of Expenditure

Eligibility of expenditure has an impact on the level of contribution from the Funds from the viewpoint of time restrictions and type of expenditure.

Time restrictions mean that expenditure shall be eligible for a contribution from the Funds if it has actually been paid after the date of submission of the OPs to the Commission or between 1 January, 2007 (whichever is earlier) and 31 December, 2015.<sup>29</sup> From the viewpoint of PPP it is an important

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<sup>28</sup> [http://www.strukturalni-fondy.cz/upload/1085590176cba\\_cz\\_ek.pdf](http://www.strukturalni-fondy.cz/upload/1085590176cba_cz_ek.pdf) (Annex B: Discount rate selection)

<sup>29</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 55(1)

condition due to the long-term character of PPP projects, specifically in the preparatory, investment and operational phases.

The rules on the eligibility of expenditure in the new programming period shall be laid down at the national level subject to the exception provided in the specific regulations for each Fund.<sup>30</sup> This is a change which may significantly impact the level of contributions from the Funds. Depending on the Fund, the following expenditure is not eligible:

- for the ERDF<sup>31</sup>:
  - a) interest on debt;
  - b) reimbursable VAT;
  - c) non-reimbursable VAT under special conditions;
  - d) costs of decommissioning of nuclear power stations;
  - e) the purchase of land for an amount exceeding 10% of the total eligible expenditure;
  - f) housing in exceptional circumstances and reconstruction of social housing within the framework of integrated operations of urban development.
- for the ESF the same expenditure as in the case of the ERDF under letters (a)-(c), and also<sup>32</sup>:
  - g) purchase of furniture, equipment, vehicles, infrastructure, real estate and land;
  - h) remuneration and salaries paid by a third party in favour of the operation participants not confirmed by the beneficiaries;
  - i) in the case of grants, indirect expenditure up to 20% of direct costs, if not posted in the books of the beneficiary, or indirect costs exceeding 20% of direct costs;
  - j) depreciable assets allocated exclusively for the duration of operation under the condition that public funds were used to acquire such assets.
- for the CF expenditure under letters (a)-(d), plus<sup>33</sup>:
  - k) the purchase of land for an amount exceeding 10% of the total eligible expenditure;
  - l) housing without any exceptions.

#### 2.1.2.4 Project Sustainability

An important factor impacting the amount of contributions from the Funds is the condition of project sustainability. The Member State shall ensure that within five years of the winding-up of the project, the operation does not undergo a substantial modification affecting its nature or giving to a firm or a public body an undue advantage resulting either from a change in the nature of ownership or an item of infrastructure or the cessation of a productive activity.<sup>34</sup>

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<sup>30</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 55(3)

<sup>31</sup> Council Regulation on the ERDF, Article 7

<sup>32</sup> Council Regulation on the ESF, Article 11

<sup>33</sup> Council Regulation on the CS, Article 3

<sup>34</sup> Council Regulation laying down general provisions on the ERDF, the ESF and the CF, Article 56(1)

## **2.2 Analysis of the Commission Documents in relation to PPP Projects**

### **2.2.1 Community Strategic Guidelines**

The Community Strategic Guidelines integrate the PPP principles into significant factors supporting proper functioning of the cohesion policy.

With respect to PPP the document defines advantages of PPP, conditions of proper PPP functioning and recommendations for use of the Funds and participation of European institutions in preparation and implementation of PPP projects.

Advantages of PPP:

- better quality of project activities and management;
- the public sector gains access to a range of private sector skills that should enable it to provide a more efficient and cost-effective service;
- the private sector takes on a range of risks that under traditional public procurement would be borne by the public sector;
- greater efficiency can be generated where a single party is responsible for design, construction, management and financing as a part of an integrated package.

Conditions of appropriate functioning of PPP:

- putting in place of an appropriate legal framework governing the project before contracting out the provision of goods and services;
- explicit policy commitment by national governments to involve the private sector in public sector projects;
- clear and specific frameworks for PPP in different policy areas, these will vary, for example, according to how far costs can be recovered through user charges and the extent of social objectives.

Recommendations for PPP implementation:

- support of PPP projects by providing finance, via the Structural Funds and the Cohesion Fund, where the projects meet all the necessary criteria;
- assessment of suitability to use PPP for small and larger projects;
- participation of the European Investment Bank (EIB) and the European Investment Fund (EIF) in the preparation and implementation of PPP projects.

### **2.2.2 Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions**

The Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions (hereinafter the “Green Paper”) is considered to be the most systemic document describing PPP on the EU level from the viewpoint of legal arrangements on the Community and national levels.

The first chapter defines PPP and formulates conditions under which public-private partnerships are implemented.<sup>35</sup> An important factor is (also when considering possible co-financing of PPP projects under the Funds) that PPP may not be a solution for budget constraints of the public sector. It is necessary to assess separately for each project, whether the partnership option offers real value added compared with other options, such as the conclusion of a more traditional contract.<sup>36</sup>

As part of the analysis of legal justification, the Green Paper proposes to make a distinction between:<sup>37</sup>

- PPPs of a purely contractual nature, in which the partnership between the public and the private sector is based solely on contractual links;
- PPPs of an institutional nature, involving co-operation between the public and the private sector within a distinct entity.

### 2.2.2.1 Purely Contractual PPPs

Purely contractual PPPs (chapter 2 of the Green Paper) refer to a partnership based solely on contractual links between the different players where one or more tasks are assigned to the private sector partner.<sup>38</sup>

In this part the Green Paper defines also such purely contractual PPPs, procedures of awarding contracts (such as use of a competitive dialogue in the case of public procurement), procedures for particular cases when the private sector has the opportunity to take the initiative in a PPP project, procedures for selecting a private partner, distribution of risks among partners, definition of the performance period, setting up parameters for changing PPP relations, as well as of rules for transferring a part or the whole public contract or concession to other contracting partners (sub-contractors).<sup>39</sup>

*Legal arrangements of the Czech concept of purely contractual PPPs correspond to the classical concept of public contracts where a contract is concluded by and between a (public) contracting authority and a (private) contractor. This model in relation to PPP in its specific form is expressed in the Concession Act (see chapter 2.3.6).*

### 2.2.2.2 Institutionalised PPPs

Institutionalised PPPs involve the establishment of an entity held jointly by the public partner and the private partner with the task of ensuring the delivery of a work or service for the benefit of the public. This allows the public sector to retain a relatively high degree of control over the development of the projects and to develop its own experience of running the service in question.<sup>40</sup>

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<sup>35</sup> Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, Articles 1-20

<sup>36</sup> Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, Article 5

<sup>37</sup> Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, Article 20

<sup>38</sup> Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, Article 21

<sup>39</sup> Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, Articles 21-52

<sup>40</sup> Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, Articles 53-54

An institutionalised PPP can be put in place either by creating an entity held jointly by the public sector and the private sector, or by the private sector taking control of an existing public undertaking. These procedures are developed in the Green Paper in greater detail from the legal point of view on the Community and national level, from the view point of awarding a public contract or concession to entities when these entities are only in the course of being incorporated and from the viewpoint of transparency and equality of treatment when selecting a private sector partner.<sup>41</sup>

*The Czech law (similarly to the Community law) does not explicitly govern institutionalised PPPs and it can be said that certain elements mentioned in the Green Paper are not possible and they would require more extensive amendment of the legislation which governs handling of public service corporations.*

*As for problems with awarding a public contract or concession to entities which are only in the course of being incorporated, the question is to which extent the position of the Commission (as per Article 10 of the Green Paper, the Commission does not recommend this procedure due to risks related to lack of transparency of the selection and functioning, ambiguities when defining the subject matter of the contract, duration of the entity and contract) will be decisive for further development of this legal instrument. In the Czech Republic, the concept of special purpose vehicles (SPV) has become an integral part of the Concession Act as an instrument facilitating PPP projects. Unlike the description of the Green Paper, the SPV under the Concession Act does not bid for a contract and all qualification criteria are met by a different entity (usually the SPV owner) and the concession agreement is then awarded to this SPV instead of the winner of the concession procedure – for more see chapter **Chyba!** **Nenalezen zdroj odkazů.***

### 2.2.3 Guidelines for Successful Public-Private Partnerships

The Guidelines for Successful Public-Private Partnerships is a descriptive and clarifying document on PPP and its application in practice without a conditional link to the Community or Member State laws and co-financing under the Funds.

The Guidelines distinguish three basic principles when defining types of PPP projects:

- approach involving traditional public procurement;
- approach involving integrated project development and operation;
- approach involving also project financing.

One must keep in mind that such classification is not absolute and constant. There is no clear classification of PPP projects generally accepted on the international level and also it is a dynamic topic bringing about new options.

#### 2.2.3.1 PPP based on Traditionally Procured Projects

In these cases the project is initiated exclusively by a public body that is at the same time the only entity which provides financing. The project is realised by an institution based on public procurement and as soon as completed it is operated and maintained again by the public body.<sup>42</sup>

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<sup>41</sup> Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, Articles 53-69

<sup>42</sup> Guidelines for Successful Public-Private Partnerships, Chapter 3.1

The most frequent type is a design-build (DB) scheme where the public body prepares a plan, ensures financing and once the project is implemented by a private entity the public body operates and maintains the project.

The private sector may be involved in the project also in other phases, in the form of service contracts or even deeply in the form of operation and management contracts where contrary to the first case the responsibility for managing the contract is transferred to a private sector partner.<sup>43</sup>

A specific case is the involvement of the private sector in investment in the form of lease. Lease contracts are different from operations and management contracts in that they transfer commercial risk to the private sector partner.<sup>44</sup>

When compared with the classification per the Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions these projects represent purely contractual PPPs.

### 2.2.3.2 PPP Integrating Project Development and Operations

In these cases a part of responsibility is transferred to the private sector partner, namely in the building and operational phases (and/or also design). It is called a build-operate-transfer (BOT) scheme or its version extended by design the design-build-operate-transfer (DBOT) scheme. The integration approach towards building and operation is provided for by detailed calculation of the life cycle and stronger involvement of the private sector in the efficient project solution.<sup>45</sup>

When compared with the classification of the Green Paper, these projects are both purely contractual PPPs and institutionalised PPPs (depending on the partnership structure).

### 2.2.3.3 PPP Involving also Project Financing

As following from the title, projects in this category allow for partial project financing by the private sector partner. These PPP structures are advantageous in particular because they offer implementation and operating advantages of the previous models with new capital resources.<sup>46</sup>

The most frequent model of such co-operation is the design-build-finance-operate (DBFO) concession agreement. These agreements enable a private investment partner to finance, construct and operate an infrastructure in exchange for the right to collect the associated revenues for a specified period of time. The ownership of all assets remains with the public sector.<sup>47</sup>

Another model is private divestiture which involves the sale of assets or shares of a state-owned entity to the private sector. Divestitures can be complete (the sale of entire assets of a utility to a single investor, or a group of investors, or through a management buyout) or partial (the Government would retain ownership of a certain portion of the former public company's assets).<sup>48</sup>

From the viewpoint of the Green Paper, concession agreements and private divestitures are only institutionalised PPPs.

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<sup>43</sup> Guidelines for Successful Public-Private Partnerships, Chapter 3.1.1 and 3.1.2

<sup>44</sup> Guidelines for Successful Public-Private Partnerships, Chapter 3.1.3

<sup>45</sup> Guidelines for Successful Public-Private Partnerships, Chapter 3.2

<sup>46</sup> Guidelines for Successful Public-Private Partnerships, Chapter 3.3

<sup>47</sup> Guidelines for Successful Public-Private Partnerships, Chapter 3.3.1

<sup>48</sup> Guidelines for Successful Public-Private Partnerships, Chapter 3.3.2

Various types of PPP schemes are described in Annex No. 1 (chapter 10).

## **2.2.4 Commission Interpretative Communication on Concessions under Community Law**

The Commission Interpretative Communication on Concessions under Community Law focuses only on concessions being a specific part of PPP. It is a deep analysis of concessions, in particular from the viewpoint of their position within the Community system of law as a tool helping all stakeholders to make themselves better familiarised with concessions and concession procedures.

In 2004, the Council adopted Directive 2004/18/EC on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts and Directive 2004/17/EC coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors which replaced the original Directives 93/37/EEC and 92/50/EEC and defined more accurately the term and field of activity for public works contract, public service contracts as well as works concessions and service concessions. (These legal acts were transposed to the legislation of the Czech Republic following the rules of primary legislation of the Community, i.e. by amendment of the Public Procurement Act and the concession bill.)

Other requisites of the Interpretative Communication were replaced by new formulations in Directives 2004/18/EC and 2004/17/EC and are covered in the Czech legislation by provisions of the Concession Act (see chapter 2.3.6)

It must be said that the document dates back to February 1999 when the only definition of concessions was mentioned in Directive 93/37/EEC on public works contracts. Other types of concessions, in particularly service concessions are based on the definition of public service contracts described in Article 1 of Directive 92/50/EEC. As opposed to Directive 93/37/EEC, Directive 92/50/EEC does not define service concessions directly.

The Interpretative Communication which is linked to older documents is thus slightly out-dated, in particular when referring to legislation. However, it defines some rules for concessions which are generally valid and can be used for the purposes of this study mainly in order to understand the role of a public and private sector in the concession procedure and general functioning of concession PPPs.

The most important are Community principles, such as equality, transparency and proportionality (particularly when selecting a concessionaire) and mutual recognition (a Member State accepts goods and services of providers from other Member States, if the goods and services comply with the conditions of the contracting authority's Member State).

*The Interpretative Communication is not a prescriptive document and during the latest public consultations of the Green Paper, some of the important participants of the consultation based their discussion on the idea that concessions do not have to be subject of the procurement procedure. In this respect, the Czech legislation is ahead of the Community legislation (whose review is planned for 2006) and concessions from the amount of CZK 2M are generally governed by a special act.*

## **2.2.5 Directives 2004/18/EC and 2004/17/EC**

Directive 2004/18/EC on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts and Directive 2004/17/EC coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors describe the procedures for concessions for works and services.

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Directive 2004/18/EC pays attention to the difference between public contracts (Title II – Rules on public contracts) and concessions (Title III – Rules on public works concessions). Title IV governs common procedures for design contests.

Directive 2004/17/EC defines the principles of procurement procedures for services and special rules for design contests in the area of services.

As both the directives were transposed to the Czech legal system, their contents are dealt with in the remaining chapters of this study describing the Public Procurement Act (chapter **Chyba! Nenalezen zdroj odkazů.**) and the Concession Act (chapter 2.3.6).

## 2.3 General Characteristics of the Czech Law with respect to PPP Projects

### 2.3.1 Civil Code, Commercial Code

In relation to PPP projects, the Civil and Commercial Codes are primarily comprehensive private legal norms to govern not only a contractual relation between a contracting authority (CA) and a private partner, but also among particular members of a consortium, being *de facto* a private partner. These relations shall exist within the framework of both the initial phase of a project (i.e. construction) and its key part (i.e. operation).

Neither of the legal instruments, however, deals with PPP projects in particular.

### 2.3.2 Public Procurement Act

Referring to the fact that a new public procurement act (hereinafter the “PPA”), replacing the existing Act No. 40/2004 Coll., should be adopted and enter into force in the nearest future, we will deal with the new wording only as in the approved document for discussion at the sitting No. 1076 of the Czech Parliament.

The new PPA is based on the concepts and principles included in the EU public procurement directives that have recently been reduced to two basic directives and existing supplementary directives<sup>49</sup>, whose transposition to the national law was to be ensured by the CR already upon its accession to the EU; the two new directives should be transposed on 31 January, 2006 at the latest.

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<sup>49</sup> These are the following directives:

- Directive 2004/18/EC of the European Parliament and of the Council of 31 March, 2004 on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.
- Directive 2005/75/EC of the European Parliament and of the Council of 16 November, 2005, correcting Directive 2004/18/EC on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts.
- Directive 2004/17/EC of the European Parliament and of the Council of 31 March, 2004 coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors.
- Council Directive 89/665/EEC of 21 December, 1989 on the coordination of the laws, regulations and administrative provisions relating to the application of review procedures to the award of public supply and public works contracts.
- Council Directive 92/13/EEC of 25 February, 1992 coordinating the laws, regulations and administrative provisions relating to the application of Community rules on the procurement procedures of entities operating in the water, energy, transport and telecommunications sectors.
- Commission Directive 2005/51/EC of 7 September, 2005 amending Annex XX to Directive 2004/17/EC and Annex VIII to Directive 2004/18/EC of the European Parliament and the Council on public procurement.

### 2.3.2.1 Necessity to Construe the PPA under the Community Law

When solving disputable and unclear issues related to public procurement, we shall refer primarily to the EU directives and decision-making practices of the relevant EU bodies, particularly the European Commission. Therefore, it is necessary to become well acquainted with the concept of the public procurement directives and the existing practices of the EU bodies.

### 2.3.2.2 Definition of Contracting Authorities

The obligation to award public contracts stays with CAs, i.e. this obligation stays with the entities specified as CAs in the PPA. The PPA stipulates three groups of CAs differing, among other things, by the scope of public procurement obligations stipulated in the PPA. Pursuant to the PPA, public contracts shall be awarded by the following entities:

- **Public CAs**, particularly the Government, institutions receiving contributions from the state budget, self-governing territorial units or institutions founded by territorial self-governing units which receive contributions from the State budget, as well as other legal entities founded to *address needs of public interest* (not of an industrial or business nature) that are predominantly funded or controlled by the State or other public CAs, as well as those where public CAs appoint more than one half of managing or supervisory bodies' members;
- **Subsidised CAs**, awarding above-the-threshold public works contract, or above-the-threshold public service contract related to such public works contract, funded (subsidised) with more than 50% by a *public CA*, even through another entity. On the one hand, the PPA deals with the chaining of subsidies, on the other hand, however, sub-contractors of the contractors to whom the contract was awarded are not considered subsidised CAs, provided that the contractor is not at the same time a public CA;
- **Sectoral CAs** performing the so-called relevant activities (particular types of business activities in the water, energy, transport and postal services sectors enumerated by law), the performance of this relevant activity is conditioned by the award of an exclusive authorisation, or these CAs are under direct or indirect dominant influence of a public CA.

To ensure proper application of the PPA, it is necessary to define the position of the Funds' recipients within the framework of a group of CAs. When drawing contributions from the Funds we can easily get in the situation when the CAs will have to be classified as subsidised CAs, despite the fact that they could be assessed as e.g. fully private entities falling outside of the PPA jurisdiction.

Should the CA be a subsidised CA, it is always governed by the provisions applicable to the procedure of a public CA, even if meeting the conditions of being classified as sectoral CAs.

To be able to determine the way a public CA shall act, which at the same time meets the criteria of a sectoral CA, it is necessary to specify the circumstances of the public contract. Generally speaking, if the public contract relates to particular activities, the procedures applying to the sectoral CA will be used (in case of objective doubts, however, the public CA procedure will be used).

Nevertheless, if the CA is a sectoral CA and if the public contract does not relate to the relevant activity at all, the CA is not obliged to follow the PPA at all. If it is not the case, then the PPA shall be followed solely in the case of public contracts above the threshold and even in these cases there are exceptions enumerated by law.

### 2.3.2.3 Public Contract Definition

#### 2.3.2.3.1 Public Contract Subject Matter

Basically, the PPA distinguishes between three types of public contracts: public supply contracts, public service contracts and public works contracts. This classification is important particularly to determine the price of a public contract and also for further categorisation and related rules (including the type of an applicable tender procedure) and particularly to determine whether the public contract shall be governed by the PPA at all.

#### 2.3.2.3.2 Public Contract Price

To begin with, the price of a public contract shall be provided without value added tax (all thresholds in the PPA are also free of VAT). The CA shall set the price by adding up the total prices of all parts of the public contract, if divided into several parts. In principle, division (in separate public contracts) is forbidden, should it be invented to circumvent the thresholds stipulated by the PPA and to change the classification of the public contract. Should there be other additional public contracts foreseen for the future, related to the present contract (based on an option), such foreseen additional public contracts must be taken into account. There is a new obligation, which is as follows. When determining the value of a public contract, the estimated values of similar, mutually linked supplies or services that are to be acquired by the CA during the accounting period must be added up.

In the case of a public supply contract and a public service contract the price shall be set as the total performance during the term of contract. Should the contract be for an indefinite period of time, the price shall be set for performance in 48 months.

In the case of a public supply contract or a public service contract on repeated performance, the price shall be set according to the actual price in the past year (adjusted according to the change expected in the next year) or the price is estimated for at least the next 12 months.

Definition of the price is important to establish the type of a public contract – the PPA distinguishes between public contracts above the threshold (the thresholds are defined by the PPA according to the type of contract and according to the type of CA), public contracts below the threshold and finally small-scale public contracts, if the price of a public supply contract or a public service contract does not exceed CZK 2M, or CZK 6M in the case of a public works contract.

The question is when to opt for awarding below-the-threshold contracts within the framework of a contract that would otherwise exceed the threshold: This option is admissible for parts whose individual value does not exceed EUR 1M for works and EUR 80,000 for services,<sup>50</sup> provided that the total value of the parts of public contracts awarded as below-the-threshold public contracts does not amount to 20% of the total value of the whole public contract, which is already above the threshold. Let us look at the following example, concerning a public contract on management of the facilities of a regional authority; the public contract being divided into five parts (e.g. one for each building):

Part 1:	EUR 100,000
Part 2:	EUR 83,000
Part 3:	EUR 45,000
Part 4:	EUR 40,000
Part 5:	EUR 5,000
Total:	EUR 273,000

The total amount exceeds the threshold stipulated by S. 14(2)(b) of the PPA for a self-governing territorial unit and therefore it is an above-the-threshold public contract. The threshold of 20% corresponds to the public contract worth EUR 54,600. Therefore, parts 3 through 5 can be awarded as below-the-threshold public contracts, because they do not exceed EUR 80,000. However, all these

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<sup>50</sup> As for services, this particular procedure may not be used by CAs from among utilities.

parts cannot be awarded under one contract, because the sum of their values exceeds EUR 54,600 – at most, parts 3 + 5 or 4 + 5 can be awarded under one contract.

#### 2.3.2.4 Types of Procurement Procedures

Once again, the new PPA introduces completely new types of *procurement procedures* to be selected by the CA when *awarding public contracts*, with the exception of cases where such selection is restricted by law. Unlike the existing PPA, the new PPA will regulate both types of negotiated procedures to make it a more standardised and less frequently challenged public procurement method.

##### 2.3.2.4.1 Open Procedure

*Open procedure* is launched upon publication of a contract notice. Any person, without being obliged to ask the CA for permission, may submit a tender. An unlimited number of contractors may submit their tenders within the given time limit; the tenders will be evaluated provided that they meet all qualification criteria.

##### 2.3.2.4.2 Restricted Procedure

Within the framework of a *restricted procedure* the CA will announce to an unlimited number of contractors its intention to award a *public contract*. Subsequently, the contractors may submit their requests for participation. From the submitted requests, the CA will select at least five candidates (a sectoral CA may select three candidates only) that have met the qualification criteria. The selected candidates are subsequently invited to submit their tenders. The number of candidates must be restricted in accordance with the pre-arranged criteria. Refusal of a candidate due to the restricted number of participants shall be announced by the CA to the candidate in writing, stating the reason. The motivation for the use of a restricted procedure is particularly the complex nature of a public contract and the anticipated scope of tenders whose evaluation is also demanding – the goal is to reduce costs of the procurement procedure by means of avoiding double selection.

##### 2.3.2.4.3 Negotiated Procedure with Publication

*Negotiated procedure with publication* is a simplified procedure to be used solely under extraordinary circumstances enumerated by the PPA (e.g. where it is impossible to pre-arrange the price of public works or services and where only incomplete tenders were submitted in *an open procedure* or *restricted procedure* and the CA has not substantially changed the technical specifications) and also for the types of public contracts specified in the Annex of the PPA (applicable to public CAs). The commencement is announced to an unlimited number of contractors (commencement by publication). Subsequently the CA invites to negotiations at least three qualified candidates that applied for participation. After submission of tenders the CA may once again reduce the number of tenderers and invite them to negotiate the tenders.

In Europe, despite the fact that it is considered as something extraordinary in the CR, the above described type of procedure is used most often in relation to PPP public procurement, because it enables step-by-step reduction of the number of tenderers in individual phases of negotiations by means of further specification of the subject matter of the public contract. On the other hand, the PPA forbids changing of technical conditions which may reduce the effectiveness of negotiations; in this respect a competitive dialogue seems to be more flexible, which, however, is accessible only to public CAs and does not allow reducing of the number of tenderers.

##### 2.3.2.4.4 Negotiated Procedure without Publication

This type of tender procedure may be used solely in the cases stipulated by the PPA, e.g. if no tenders were submitted in *an open* or *restricted procedure* that would meet the technical specifications; in the case of an additional supply; a public contract that can be performed solely by a particular contractor; a public contract awarded in emergency; if it is an extraordinary bargain, etc. The CA shall invite a

selected group of candidates to submit their tenders. Subsequently, based on the results of negotiations, it shall choose the winner.

#### 2.3.2.4.5 Competitive Dialogue

If a public CA is not capable of specifying technical conditions or legal and financial requirements with respect to the performance under the public contract, it can use a competitive dialogue, during which the terms and requirements are specified on an ongoing basis until the candidates can be invited to submit their tenders. Once the qualification phase is over, the public CA is obliged to invite at least three candidates to participate in the competitive dialogue.

A drawback of the competitive dialogue as described in the PPA for the PPP is the fact that it is only the number of solutions what can be restricted rather than the number of tenderers. It means that all tenderers of a dialogue must be invited to submit their final tenders pursuant to the conditions that arose from the dialogue – the CA is thus obliged to perform time-consuming evaluation of the final tenders, usually from three tenderers (in European countries, however, two or even one tenderer often participate in the final negotiations).

#### 2.3.2.4.6 Simplified Procedure for Below-the-Threshold Contracts

In the case of below-the-threshold public supply or service contracts or in the case of below-the-threshold public work contracts with a value of up to CZK 30M, the public CA may use a simplified procedure (*de facto* falling out of the scope of the European directives). In principle, this is an equivalent of the negotiated procedure without publication (the obligation to address at least five candidates, and always a different group of candidates, if possible) with the difference that the call is published in an appropriate manner in the course of the tender period.

#### 2.3.2.5 National Public Procurement Checks

Public procurement check mechanisms may be divided into internal and external ones. Within the framework of *internal* checks, such check mechanisms are applied by the public CA, so that the performance of powers of relevant subordinate units or employees complies with both statutory and internal standards. In this respect we can say that with regard to the principle of primary control by a Member State (see the next chapter) it will be necessary to introduce efficient check mechanisms to avoid breaching of the regulations on the internal level, if possible. The mechanisms that have already been introduced will have to be revised.

*External* control is conducted particularly by the Office for the Protection of Competition (not to mention other aspects of the government control applied by other administrative bodies) using a review procedure to review the CA actions. This process does not contain any specifics applying to the PPP.

#### 2.3.2.6 Public Procurement Checks by the Commission

The following paragraphs are based on the general principles of monitoring and control of the Funds expenditure. They also reflect a possible recourse following violation of binding rules applicable to the funds. The areas of monitoring, control and rectification are covered by basic legal instruments of particular funds. However, we cannot use the word “individually”, because their principles are identical and deviations, if any, occur only where required by the specific nature of the fund (most frequently in the method of verification of cost eligibility or the method of penalty calculation).

The most important legal instruments governing the framework and general issues are as follows:

- Council Regulation (EC, Euratom) No. 1605/2002 of 25 June, 2002 on the Financial Regulation applicable to the general budget of the European Communities;

Final Report on Project 1p/05 – “Application of the PPP Principle on the Economic and Social Cohesion Policy” dated 15 May, 2006

- Commission Regulation (EC, Euratom) No. 2342/2002 of 23 December, 2002 laying down detailed rules for the implementation of Council Regulation (EC, Euratom) No. 1605/2002 of 25 June, 2002 on the Financial Regulation applicable to the general budget of the European Communities;
- Commission Regulation (EC, Euratom) No. 2343/2002 of 23 December, 2002 on the framework Financial Regulation for the bodies referred to in Article 185 of Council Regulation (EC, Euratom) No. 1605/2002 on the Financial Regulation applicable to the general budget of the European Communities;
- Council Regulation (EC, Euratom) No. 2988/1995 of 18 December, 1995 on the protection of the European Communities financial interests.

For a moment we shall stay with the last Regulation, because it stipulates the rules of performance of checks and it is referred to by the sectoral regulations. This Regulation provides a definition of the word “**irregularity**” in the first place, which is something that needs to be avoided and therefore penalised. Article 1(2) of this Regulation stipulates that the “irregularity” shall mean any infringement of a provision of Community law resulting from an act or omission by an economic operator, which has, or would have, the effect of prejudicing the general budget of the Communities or budgets managed by them, either by reducing or losing revenue accruing from own resources collected directly on behalf of the Communities, or by an unjustified item of expenditure. It is therefore obvious that pursuant to this Regulation any drawing on the Funds performed in breach of the Community law shall be penalised. As concerns the reference to the Community law, we need to emphasise one part of the text that may be misleading – with respect to the fact that the relevant regulations governing particularly the Funds often require Member States to ensure particular checking standards in order to detect irregularities and some obligations related to such detection may be specified by a national implementing regulation, a specific default and occurrence of irregularities may be related to infringement of a particular national regulation. Nevertheless, this should not be mistaken with more strict rules that Member States are authorised to apply – this would not be linked to the Community law and therefore an irregularity would not be committed within the meaning of the Regulation and would not fall within its jurisdiction.

The checks (procedures) are subsequently conducted pursuant to the below rules, however, they are often adjusted pursuant to sectoral regulations and also according to a body or institution performing the check, as the case may be.

Regulation No. 2988/1995 further stipulates a key aspect of checks, i.e. **duration of limitation periods**. The limitation period for proceedings shall be four years as from the time when the irregularity was committed; however, the sectoral rules may make provision for a shorter period which may not be less than three years. The Funds discussed in this document do not stipulate this period specifically, they only stipulate the obligation to archive necessary documents for a period of three years. In the case of continuous or repeated irregularities, the limitation period shall run from the day on which the irregularity ceases. In the case of multi-annual programmes, the limitation period shall in any case run until the programme is definitively terminated. However, limitation shall become effective at the latest on the day on which a period equal to twice the limitation period expires (i.e. in most cases within eight years), however, also this period can be extended, provided that criminal proceedings are instigated against the person in question concerning the irregularity. The period for implementing the decision establishing the administrative penalty shall be three years. Member States, however, shall retain the possibility of applying a longer period.

The Regulation further stipulates the **principle of penalties**, i.e. removal of an advantage wrongly received (the Regulation uses the term “administrative measure”), which is reflected in the institute of financial corrections of both funds. In addition to that, intentional irregularities or those caused by negligence may lead to other penalties (fines, exclusions, etc. – for details see Article 5 of the Regulation).

To conclude, the Regulation stipulates the principle that it is primarily a **Member State’s responsibility to perform checks**, i.e. the checks performed by EC bodies and institutions are considered to be ex-post checks – irregularities, if found, are then presented as failures of control mechanisms falling within the responsibility of the Member State. In the case of the Funds, this subsequently affects net revenues of the entire Member State from a particular fund. At the same time the control mechanisms should not place an unnecessary burden on business entities; simultaneously it is necessary to avoid disproportionate cost of administration proceedings.

#### 2.3.2.7 Links to PPP Projects

The new PPA stipulates that in addition to the use of the relevant provisions of the PPA, a special additional amendment to the Concession Act may be applied, provided that an above-the-threshold public contract will be concluded for a period **over five years** and the contractor will bring **part of the economic risks** related to the implementation of the public contract that is usually borne by the CA.

In such case special essentials of a concession agreement are defined: the option of the contractor to collect fees from the users of services rendered by the contractor (concessionaire) if they could otherwise be provided by the CA; the option of the CA to accept an obligation of future performance which is not covered by the CA budget valid at the moment of contract conclusion; liability of the CA for damage caused to service users by the concessionaire.

Furthermore, a concession project must be elaborated and approved and the concession agreement is subject to approval as well (by the Government, regional or municipal council, according to the nature of the CA).

For more details about the Concession Act see chapter 2.3.6.

### 2.3.3 Act on the Property of the Czech Republic

As regards public contracts to which the PPP method shall apply, we should take into account particular restrictions stipulated by Act No. 219/2000 Coll., on property of the Czech Republic and acting of the State in legal relations. Depending on the specific terms and conditions of a project, it is necessary to count upon the fact that some parts of the project will be related to the property of the State and therefore it will be necessary to respect the relevant property handling rules.

One such restriction is the fact that some items and values can be owned solely by the State. Such items and values are stipulated by special acts. These acts, in addition to the property of the State, may define also other property, e.g. regional or municipal, and therefore it will be necessary to deal with this aspect always *ad hoc*, depending on a particular project.

As regards the setting of the price for the transfer for consideration of a particular item to the ownership of the State (depending on the PPP model this will occur at various moments of the project life cycle), we assume that the existing rule will apply that the price will not have to comply with price regulations, because it will be based on the outcome of an award or concession procedure (unless the negotiated procedure without publication is used).

An important restriction applying to a “usual” public contract is that the investment threshold may not be circumvented by concluding contracts of lease, while in the case of concession agreements this restriction will not apply.

Transfers of property of the State to the hands of other persons are complicated by the fact that unless the property is absolutely unneeded, such transfers must be approved by the Government due to serious reasons only (we assume that in the case of a PPP project such reason would be ascertained) and only with prior approval of the Ministry of Finance. In addition to that, this restriction is linked to

the ban on the contractual right of lien, which, however, is not absolute, because the ban applies neither to the purposes of infrastructure development or operation, nor to development in the public interest; everything else is subject to approval.

A more passable way is the use of lease, because things may be given over for enjoyment provided that they are used in a more efficient and economic way while retaining the main purpose which the thing serves (the State). A restrictive factor for the PPP projects is the maximum duration of a contract of lease which is stipulated by law for five years; the contract of lease, however, may be renewed after such a period elapses – due to serious reasons, exceptions may be approved by the Ministry of Finance. Sub-leases, if any, shall be approved by the founder or appropriate central administration office.

### **2.3.4 Regional and Municipal Structures**

Pursuant to S. 18 of Act No. 129/2000 Coll., on regions, a precondition of the validity of a legal act performed to change a title to regional assets is to make such act public on an official board “to enable the candidates to raise their opinions and submit their tenders”; this should be done within at least 30 days after the relevant regional authority makes its decision. The question now is whether the precondition of publication will be met by the public nature of the very procurement/concession proceedings, or whether it will be necessary to perform special acts that might complicate the time schedule of the procurement/concession proceedings. A particularly counterproductive aspect would be if such acts were to reflect current conditions negotiated at the individual stages of the negotiated procedure or competitive dialogue. The same can be said about the identical duty imposed on municipalities pursuant to S. 39 of Act No. 128/2000 Coll., on municipalities.

### **2.3.5 Budgetary Rules**

Act No. 218/2000 Coll., on budgetary rules and amendments of some related acts (the budgetary rules) will be amended in line with the Concession Act only in the provisions governing the mid-term outlook, in order to reflect a future burden arising from all concluded concession agreements. In this respect, it is particularly important that the liabilities arising therefrom are included in the mid-term outlook regardless of the duration of concession agreements.

What is strange, however, is that Act No. 250/2000 Coll., on budgetary rules applying to territorial budgets, should not be amended in a similar way, which would *de facto* enable regions and municipalities to conceal actual amounts of all liabilities arising from concession agreements, provided that the current 5-year maximum after the budgetary year is included in the budget outlook.

From the viewpoint of PPP projects, there is one important indirect amendment to the budgetary rules by the Concession Act, ensuring that CAs have the option to undertake themselves to future performance not covered by the CA budget valid at the moment of concluding the agreement.

### **2.3.6 Legislation Governing Concessions and PPP Rules**

The new bill on concession agreements <sup>51</sup> (hereinafter the “Concession Act”) introduces to the national legislation a specific regulation that should provide a framework for all the above specified methods of public procurement corresponding to the PPP definition and related issues pertaining to the approval of such public contracts.

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<sup>51</sup> Document for discussion at the sitting No. 1078

In other words, the Concession Act shall be used if the public contract is awarded by a public CA and if the subject matter of such public contract is provision of services or performance of work by a concessionaire, that will then be able to enjoy benefits from the provision of services, or to use the performed work, which could be complemented by other payments by the CA to the concessionaire; at the same time it is the concessionaire that bears a substantial part of risks related to the enjoyment of benefits from the provision of services or use of the performed work. However, if applied, the Concession Act will to a certain extent use the reference in the PPA discussed previously in chapter 2.3.2.7. In other words, should the result of public procurement be a PPP project, the Concession Act will eventually be used. At this point of time, however, we can assume that the exact border between a common public contract and a PPP project is yet to be established when construing provisions of S. 156 of the PPA.

### 2.3.6.1 Concession Definition

The subject matter of a concession agreement has been specified above, because in the Act it overlaps with the very scope of application of the Concession Act. For the Concession Act the classification according to types is of no significance; occasionally, there are *ad hoc* terms and conditions stipulated for e.g. concession agreements on construction projects, works, etc.

As opposed to public contracts, concession agreements may only be concluded for a definite period of time. On the other hand, however, CAs may conclude a concession agreement to perform in the future, even if the performance is not covered from the CA budget at the moment of conclusion of the concession agreement. It is a special provision that must be construed along with the regulations applying to budgetary rules.

The option of sub-concessions (even partial) is excluded – this provision prevents transfers of primary rights and obligations to other entities; it does not mean, however, that the concessionaire cannot procure some parts of the concession agreement through sub-contractors. For these purposes it is necessary to distinguish between common sub-contracting and a sub-concession (an agreement whose characteristics are those of a concession agreement). Responsibility for damage caused by the concessionaire to users in direct relation to the provision of services stays always with the CA. Therefore, the concession agreement must deal with regression claims of the CA with respect to the concessionaire.

To specify financial matters pertaining to the concession agreement, it is necessary to establish the value of the subject matter of the concession agreement as well as the estimated revenue of the concessionaire. The essential rules of calculating the values are stipulated by an implementing regulation that has not been published yet and whose original draft does not correspond to the changes of the Concession Act as discussed by the House of Deputies. We assume, however, that a total amount of all liabilities arising from the concession agreement throughout its whole duration will be taken as the value of the concession agreement subject matter. If the suggested method of calculation is adopted (i.e. pursuant to Article 9 of Directive 2004/18/EC), the rules will then not differ from the calculation method stipulated by the PPA. The rules will determine the calculation of the concessionaire’s estimated revenue, having consequences for the drawing on the Funds.

Only for the purposes of a special rule applying to sub-contracting, the Act defines above-the-threshold concession agreements on construction projects, provided that the estimated value of an agreement, whose subject matter is a construction project, exceeds CZK 165,288,000.

### 2.3.6.2 Concession Proceedings

The concession agreement, where the estimated revenue of the concessionaire is equal to or exceeds CZK 20M, may be concluded once the concession proceedings have taken place. The procedure, in

spite of being governed by a specific provision, is in many aspects governed by the provisions of the PPA, to which the Concession Act often refers.

A concession proceeding is always initiated by the call to participate in the first round, in which contractors must prove their qualifications. The number of contractors to participate in the next round may be limited in the first round pursuant to the PPA rules. As for the second round, the CA may opt for one of the three possible procedures: (i) submission of tenders and their evaluation; (ii) submission of tenders and commencement of negotiations on the tenders (an equivalent of the negotiated procedure with publication); (iii) participation in the concession dialogue as a process of finding the most suitable solution (an equivalent of the competitive dialogue); the concession dialogue may be continued with using method (i) or (ii). Please note that concession proceedings applying to the so-called major concession agreements feature yet another aspect – preparation and approval of the concession project and concession agreement, discussed in chapter 2.3.6.4.

For the final selection of a concessionaire based on submitted tenders, only the economically most advantageous tender criterion can be used, which is also governed by the PPA, i.e. certain criteria shall be assessed, such as price, quality, environmental impact, operating costs, return on costs, service, delivery terms. In the case of PPP projects a role will be played by e.g. division of particular risks among the CA and the concessionaire, amount of payment for provided services, availability, etc.

As opposed to the PPA, the Concession Act uses the institute of the special purpose vehicle (the so-called SPV) a special legal entity founded to perform the tasks of a concessionaire. In the case of public contracts – in the classical meaning of the word – the SPV could not have any experience and track record to meet the qualifications. However, if the SPV is directly or indirectly controlled by the selected contractor and if the subject matter of its activities dwells in implementation of the subject matter of the agreement, the concession agreement can be concluded directly with the SPV.

### 2.3.6.3 Sub-contractors

Engagement of sub-contractors, non-members of the concern, may slightly hinder the commencement of a PPP project, because the Concession Act requires that the privately-owned concessionaire performs some special duties. In the case of an above-the-threshold concession agreement for works the part of the public contract whose value exceeds CZK 165,288,000, must be awarded in the form of a certain public procurement procedure, whose only legal precondition is to publish the intention and allow 40 days for tender submission – pursuant to the justification report to the Concession Act this should have been transposition of Articles 63 through 65 of Directive 2004/18/EC; however, it is clear now that Article 65, if not other things, was not transposed well, particularly when it comes to classification of time limits of qualification and tender periods and also when it comes to the possibility to shorten or the obligation to extend the time periods. Particularly the absence of the possibility to shorten the time periods should be considered a serious defect potentially damaging the concessionaire. There are no further requirements applying to the course of negotiations with respect to a contract with the sub-contractor.

In addition to that, the CA may require that in the case of above-the-threshold concession agreements on works the concessionaire has to sub-contract at least 30% of works to third persons, which gives the CA the possibility to exact the procedure specified above, regardless of its effectiveness.

### 2.3.6.4 Concession Project and Concession Agreement Approval

The Concession Act defines a special group of the so-called major concession agreements, these being related to the estimated revenue of the concessionaire and also to the nature of the CA (accordingly, financial thresholds vary from CZK 50M to 500M). In the event of a major concession agreement, before the concession proceedings is initiated (or prior to the call for tenders, provided that the concession dialogue is used) it is necessary to develop and approve a concession project whose

essentials are stipulated by implementing regulations; the following essentials can be expected: description of the service rendered by the concessionaire, description of the work performed by the concessionaire, estimated time schedule of concession agreement implementation, financial resources for the concession agreement implementation, distribution of economic risks among contractual parties, impacts upon public budgets, proposed method of control of the CA over the concession agreement performance, economic impacts upon agreement termination, proposed distribution of legal risks among contracting parties, payment terms, legal instruments of the concessionaire’s control, proposed security, if any, proposed settlement upon termination of the concession agreement by the elapse of time or another way (e.g. withdrawal, mutual agreement), proposed final settlement upon termination of the concession agreement, legal impacts of the contract termination. The concession project is either approved by the Government, regional or municipal council, or a body responsible for economic activities of the CA – depending of the type of the CA.

In the above cases, the concession agreement, once the concessionaire is selected, is approved by the Government, region, municipality, or a body responsible for economic activities of the CA – depending on the type of the CA; the approval being a necessary precondition of the validity of the concession agreement. If the agreement is not approved, the CA shall cancel the concession proceedings.

Should the agreement be amended during its effective period, and should the estimated revenue of the concessionaire increase, the following situation may arise: 1) the change of the concession agreement, which has already been approved as a major concession agreement, will have to be submitted for approval, provided that the estimated revenue grows by more than 20%, or 2) due to the change the concession agreement becomes a major concession agreement and subsequently it will be necessary to submit it for approval as a whole, including the change.

#### 2.3.6.5 Supervision

Similarly as for the Public Procurement Act, fulfilment of obligations arising from the Concession Act will be supervised by the Office for the Protection of Competition, using the full scope of its powers (recourse measures, fines). Similarly, the PPA shall govern the filing of objections in the concession proceedings and reviewing of the CA’s course of actions.

In addition to that, however, the Ministry of Finance has the power to perform special budget supervision over territorial self-governing units (and their “subordinate” organisations receiving contributions from their budgets, as well as other legal entities). The ministry, however, has no power to issue orders, because the supervision is performed in the form of opinions with respect to concession agreements. The opinion containing assessment of possible impacts of the concession agreement commitments on the economic situation of the CA must be mandatory discussed when approving the concession agreement, however, in the case of “minor” concession agreements, no obligation is stipulated for the CA to take it into serious account. We can only guess what consequences a failure to regard the opinion would have, since neither the Concession Act nor other regulations stipulate any sanction provisions.

The Ministry for Regional Development maintains a registry of all concession agreements, the CAs are obliged to notify it within 30 days after the agreements enter into effect. The agreements are kept in the registry until the concession agreement expires.

#### 2.3.7 Competition Law Issue

Within particular PPP projects (referring to the subject matter of the projects) a situation may arise when the concessionaire (selected as the only one for a given project) gets in the position of a dominant competitor. In such case it is necessary to take into account that such a concessionaire may be subject to a procedure initiated by the Office for the Protection of Competition, because the

dominant position is quite often abused (inadequate prices for rendered services, provision of services conditioned by the provision of other services, using different terms and conditions for different service users, limited service provision, inadequately low prices). Due to variety of types and structures of PPP projects, as well as the forms of abuse of one’s dominant position, it would be inefficient to create special rules applying to PPP projects in the area of competition law.

As for this issue, we may refer to conclusions of chapter 2.3.8.5

### 2.3.8 State Aid Issues

In many cases, more complex PPP projects may involve banned state aid. Below is provided a general description of the state aid concept and recommendations how to limit possible risks arising from the provision of banned state aid within the framework of PPP projects.

#### 2.3.8.1 State Aid Definition

The ban on (“incompatibility”) and definition of state aid are stipulated by Article 87(1) of the EC Treaty. The definition reads that any aid granted by **a Member State or through State resources in any form** whatsoever which distorts or threatens **to distort competition** by favouring **certain undertakings** (most often business entities) or the production of certain goods (both goods and services) shall, insofar as it **affects trade between Member States**, be incompatible with the common market.

As to determine where state aid is or is not involved, we need to consider the **effect** of an action, not its decisive declared objective.

As for classification of particular entities falling within the term “State”, the European Court of Justice (hereinafter the “**ECJ**”) concluded that the term “State” included territorial self-governing units, as well as legal or natural entities falling within the jurisdiction of the public law.

#### 2.3.8.2 *De Minimis* State Aid

There are state aid rules which enable provision of state aid amounting up to EUR 100,000 to a single entity in the course of up to three years under the so-called *de minimis* principle. Such aid may be provided without prior notification and affirmative decision of the Commission.

#### 2.3.8.3 Rules of Land and Building Transfers to Public Entities

It cannot be excluded that the structure of PPP projects will require the State to make a contribution in the form of State-owned real estate transferred to the hands of legal persons whose activities will constitute a major part of a PPP project. Having regard to certain specific state aid issues related to land and building transfers to public law entities, the Commission has issued a Memorandum describing the methods of transfer of land and buildings owned by public law entities, automatically excluding state aid.

The purpose of the Memorandum is to enable public law entities to proceed efficiently and promptly while transferring real estate without the necessity to undergo a relatively complex and demanding notification procedure as described below.

In general, we may say that from the viewpoint of state aid, the Commission deems acceptable only such real estate transfers that are performed based on (i) public tender with multiple tenderers or (ii) appraisal by an independent expert.

#### 2.3.8.4 State Aid Procedure before the Commission

The procedure before the Commission with respect to state aid is governed by Article 88 of the EC Treaty, Council Regulation No. 659/99 and Commission Regulation No. 794/2004. Council Regulation No. 659/99, in addition to the rights of state aid providers and beneficiaries, governs also the rights of third parties, e.g. competitors.

##### 2.3.8.4.1 Notified Aid Procedure

There is a general rule that the Commission must be notified of all new measures which constitute state aid with the exception of aid on which this obligation does not apply based on Article 89 the EC Treaty (the so-called block exceptions).

The participant of the notification procedure is solely a Member State (most frequently through its mission in Brussels); however, also the beneficiary itself may participate in the procedure in a particular way. The procedure before the Commission shall assess the compatibility with the common market. Provision of state aid must be postponed until the Commission makes a decision within two months from the submission of a full notification, stating that (i) no state aid is involved, (ii) the state aid is compatible (in such case, the Commission grants the exception based on compatibility of the aid with the common market), (iii) the state aid exists and at the same time there are justified doubts concerning its compatibility, which triggers a **formal examination procedure**. If the Commission does not provide any decision within the above specified time limit of two months, legal fiction shall apply that the state aid is compatible with the common market.

The decision to commence the formal examination procedure is published in the Official Journal of the European Union which gives space to comments of the stakeholders (e.g. due to incompatibility with public interest, unfair strengthening of an entity on the market). In addition to the involved Member State, also the other Member States, competitors or business associations may raise their comments, the beneficiary, on the other hand, may defend the state aid provision. Comments need to be delivered within one month from the commencement of the procedure and they are all sent to the Member State for comments.

Within the framework of the formal examination procedure in a period of 18 months, the Commission will decide that either (i) no state aid is involved, (ii) state aid is involved which is compatible with the common market, or (iii) state aid is involved which is incompatible with the common market.

##### 2.3.8.4.2 Illegal State Aid Procedure

The Commission's missions perform monitoring in Member States, including regional press monitoring, and handle complaints of competitors and tax payers. The Commission may also request provision of information from a Member State for assessment. Based on the above specified information sources, the Commission may, independently from the Member State, ascertain whether state aid exists or not.

If state aid was not notified or was provided prior to a decision to provide a notified state aid, the Commission will commence the illegal state aid procedure. Within the framework of this procedure, by issuing a preliminary measure, the Commission may seek **suspension** or even **provisional return** of the aid. Failure to observe preliminary measures may result in **an action** of the Commission against the Member State before the ECJ for infringement of the EC Treaty.

In the course of procedure, the Commission decides upon compatibility of state aid with the common market, as in the procedure applying to notified aid, however, the 2-month or 18-month time limits for making a decision do not apply to the Commission. There is only one time limit that the state aid must be returned within 10 years after being provided.

If a **decision on aid return** is made, the provided aid shall be returned including interest stipulated by the Commission, even in the case of bankruptcy. The Member State is obliged to return the state aid using mechanisms of the national law. In relation to the state aid beneficiary the principle of good faith is not applied; it is the beneficiary who must monitor whether the state aid received complies with the law.

If established that the aid was misused (e.g. used for a different purpose), the Commission may commence a formal examination procedure and issue a **decision on aid return**, as the case may be, including the possibility to issue a preliminary order to suspend aid provision.

#### 2.3.8.4.3 Existing Aid Programme Procedure

The programme may be a specific law, decree, regulation or internal measure including provision of aid. Such programmes are approved and continuously reviewed by the Commission which also proposes certain measures – amendments in the form of (i) programme supplements, (ii) procedural mechanisms, or (iii) **programme cancellation**. If a Member State fails to accept the proposal of the Commission, a formal examination procedure may commence.

#### 2.3.8.4.4 Interim Procedure

Article 3 of Annex IV of the EC Treaty stipulates a special procedure of the Commission to review the state aid granted in the Czech Republic before the accession of the Czech Republic to the EC, as well as that granted after the accession.

Only the following aid shall be considered existing and duly notified (i.e. the aid that can be granted also after the accession to the EU): (i) granted before 10 December, 1994, (ii) specified in a supplement to the Annex and (iii) assessed pursuant to Act No. 59/2000 Coll., on state aid, provided that the Commission has not raised any doubts (with respect to compatibility).

Upon accession, all other valid aids are considered to be new aids, i.e. they must be notified to the Commission, subject to very strict assessment, based on which the obligation could arise to stop the aid and even to **return** it.

The *interim procedure* may be used to avoid qualification of an aid as a new aid. There is a condition that the CR has submitted a measure constituting state aid, which should not be automatically considered to be existing aid after the accession, before the submission to the Commission for review, and the Commission, within three months from receiving all information, has not raised any objections and/or has initiated the formal examination procedure.

#### 2.3.8.5 Recommendations on State Aid Rules

Due to the fact that in particular cases PPP projects may be affected by certain aspects of state aid, we are convinced that due to the diversity of PPP project types and structures and due to the diversity of state aid forms it would be inefficient to develop special rules applying to PPP projects from the viewpoint of state aid.

Due preparation of a PPP project should always consist of comprehensive legal due diligence of the proposed structure, which should reveal potential state aid related risks. We believe that it is important for public institutions to be well acquainted with basic state aid instruments and solutions, e.g. notification obligation and rules of transferring land and buildings in public ownership. This relatively simple approach should help to efficiently solve state aid issues within the framework of *ad hoc* approach supported by due legal preparation of projects.

### **3 Basic Identification of Barriers and Risks for Combination of PPP and EU Funding on the General Programming Level**

#### **3.1 Legislative Barriers**

##### **3.1.1 Procedures Contrary to Law in Public Procurement**

Due to its brevity, the existing legislation governing public procurement gives rise to doubtful interpretation, which cannot be easily remedied without in-depth knowledge namely of the decision-making practice of the Office for the Protection of Competition and public procurement rules applied in the EU. Such situation results not only in the objective risk that the contracting authority may proceed contrary to law because of their own fault, but also the subjective risk that the contracting authority may misuse the vague interpretation to prefer e.g. a specific supplier. This, besides the fact that it is an illegal procedure, increases especially the risk that public procurement procedure may be cancelled by a supervisory body. The impacts are as follows: creation of a non-transparent environment and discouragement of investors, fines imposed on the contracting authority, unfulfilled objectives of a given project. Negotiated procedure with publication, often used in the European countries especially for PPP projects, is not specified in the existing Public Procurement Act in the Czech Republic.

In the case of PPP projects, particularly given the duration of a standard public procurement procedure, possible failure produces considerable inefficient costs both for the contracting authority and the candidate.

Though the new legislation stipulates the relevant procedures more precisely, the fact that it is new may cause similar difficulties at the beginning of the programming period, especially in the case of new institutes such as a competitive/concession dialogue.

##### **3.1.2 Contradiction between Compatibility of PPP and State Aid Rules**

From the legal aspect we can see no greater risk that the state aid rules would be violated in relation to the systemic application of PPP methods. Provided that the public procurement procedure took place in a strictly transparent and non-discriminatory manner, illegal state aid infringing Article 87 of the Treaty establishing the European Community should not occur.

Nevertheless, the comprehensive nature of public procurement procedures in PPP projects, during which the nature of a public contract is subject to ongoing revaluation until the final phase, may cause a certain factual risk that the state aid would be known no sooner than at the moment when other candidates are excluded from the procedure; however, they could e.g. again show interest under such changed conditions. If the short-listed parties interested in a public contract include a “local” supplier, there is a greater risk that the Commission would conduct a closer inspection of the relevant state aid aspects as to their compatibility with the single market. The said risk may be reduced by creation of such a public procurement system in which the awareness regarding potential state aid would be as broad as possible at the beginning of the public procurement procedure (without making the public contracting authority obliged to provide such aid).

### 3.1.3 Legislative Restrictions

Creation of PPP necessitates sufficient legislation particularly in the area of management and monitoring by the public sector. Feasibility of PPP is realistic under the current legal conditions. It depends on the legislators whether they would allow for a certain flexibility to modify the PPP methods depending on the given development by not enacting a special law or whether they would set clear rules which could limit a quickly adapting private sector in the changing environment. We would not describe the present situation as a restriction, but rather as a failure of the public sector to get ready for effective monitoring, including the possibilities to enforce the rules in order to prevent financial corrections by the Commission.

We recommend to review effectiveness of legislation governing public procurement and concession procedures based on experience gathered from the pilot PPP projects. It is especially the procedural part that already shows some deficiencies as regards flexibility to adapt the public procurement procedure (even when complying with the fundamental principles of this process) according to the specific features of PPP projects.

### 3.1.4 Restrictions Related to Beneficiaries and the Ownership Structure

#### Ministries as beneficiaries

In the case of projects combining a PPP model and co-financing under the Funds we may assume that in the programming period 2007-2013 the beneficiaries for grants from the Funds would be especially the ministries, regions, municipalities, their organisations which receive contributions from the state budget and organisational units, SPVs<sup>52</sup> and legal entities owned by the public entity. As for the regions and some ministries, they have already been applying the system when one of the departments of a given ministry/region is incorporated into the implementing structure (either in the role of a managing authority or an intermediate body) and other of their departments apply for grants from the Funds as beneficiaries (e.g. the Transport Department, Employment Services Administration Department and Social Services Departments at the Ministry of Labour and Social Affairs). Nevertheless, it is not a standard procedure used in all operational programmes.

For this reason we recommend, as regards the selected priorities suitable for combination of PPP projects co-financed under the Funds, to pay closer attention to identification of potential beneficiaries in order to prevent unexpected complications such as the parties submitting PPP projects not being included in the group of potential final beneficiaries.

#### SPV in public ownership as a beneficiary

The Government may either establish an SPV (see chapter **Chyba! Nenalezen zdroj odkazů.**) as a joint-stock company or may acquire a stake in the SPV. Acquisition of shares must be either in line with the pricing regulations or may take place by means of a tender. If shares are acquired through awarding of a public contract, we recommend to combine selection of a strategic partner with offer of participation in the SPV. Let's look at a model example when during project preparation the contracting authority sets up an SPV as a joint-stock company, while one of the terms of reference of a public contract (concession) would be for the consortium to submit an offer to acquire e.g. a 90% stake in the SPV. Subsequently, the selected private entity (consortium) agrees as the owner of a 90% stake in the SPV to provide (increase) the needed registered capital of the SPV in such a way so that it would successfully fulfil the subject matter of a public contract (concession). Thanks to the remaining stake in the SPV the contracting authority will be able to take part in the SPV bodies in order to have some control over the activity of the SPV and thus also over performance regarding the subject matter

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<sup>52</sup> SPV – Special Purpose Vehicle: special project entity set up for implementation of PPP projects.

of a given public contract (concession). The concession agreement should suffice to stipulate the relationship to the SPV, including ensuring of control.

The said procedure for establishing SPV is conditioned by the Government’s consent. If a state-established SPV was to become majority-controlled by a private entity, it must always be approved by the Government.

The General Regulation allows for (i.e. does not prohibit) an SPV to be a beneficiary. Nevertheless, we point out the fact that in the case of a public SPV it could be in violation of the rule to separate functions. However, specific implications will also be derived from the Commission statutory instrument governing the managing authorities.

As for exploitation of an SPV at the regional level, it is simpler as the title to ownership interests is not conditioned by consent of the Government, but only the relevant regional authorities (council, regional assembly) depending on the nature of the matter relating to the SPV.

Besides joint-stock companies, it is also possible to set up limited liability companies.

As regards the doubts sometimes raised in relation to evaluation of an SPV as a public or private entity, we may consider the following: from the legal point of view the SPV will be considered a public entity only if wholly state-owned. In any other case it must be considered a private entity. Nevertheless, this categorisation, in our opinion, has no grounds as state aid does not depend on such evaluation, but on characterisation of the SPV as an “undertaking” under Article 87 of the Treaty establishing the European Community. We may already say that in the case of PPP projects the SPV will be mostly considered an undertaking.

#### Ownership of infrastructure

As for the PPP model, project sustainability may be problematic from the point of view of ownership relations if the private investor is the owner of infrastructure. If contractual relations are not well defined, such a situation may be in contradiction with the ESC rules. Under these rules the state aid beneficiary (public entity) agrees to provide for project sustainability. Such a condition is impaired also if the ownership of the investment subject matter is altered and consequently the related project goals are not adhered to for the period of at least five years (pursuant to Article 56(1) of the General Regulation).

With regard to the said condition it is necessary to make sure that during the programming period the infrastructure ownership was transferred only to a limited extent or that such a procedure is subsequently provided for with the new owner attaining the project goals, too.

### 3.1.5 Fiche Deviation Risks

Of course, the fiche is not a binding document and therefore does not have to be adhered to in this respect. On the other hand, it is interpretation provided by the key authority – the Commission. Any deviation from the given fiche subsequently needs to be:

- in compliance with laws and regulations (especially with the regulations which the given fiche interprets);
- generally justified.

If there is some tendency to deviate from the fiche, it would be best to incorporate such a deviation already into the NSRF or an operational programme to be approved by the Commission. It gives rise to a risk that the Commission does not approve it and the OP will have to be changed.

*Compliance with project sustainability rules must be first of all stipulated by a contract and subsequently subject to functioning effective control mechanisms which would be able to identify all the changes in ownership relations. At the same time, sanctions for the event of non-compliance with these binding terms must be determined. The said rules are set for the projects drawing on the Funds; however, at this phase it is necessary to take account of specific features of the PPP model (e.g. the issue of transfer of the ownership title to a private investor after the period of project sustainability elapses without the need to amend the concession agreement).*

## 3.2 Barriers relating to the Financing Structure

### 3.2.1 Project Cash Flow

The typical feature of the PPP model is the financial involvement of the public sector no sooner than after the project output is put into operation. On the contrary, in the case of standard investment acquisition, the public sector covers the investment costs already during the investment phase of a given project and the EU grants are paid after completion of a given project phase. If a PPP project is combined with the Funds, it is necessary to find an efficient combination of cash flow related to the grants from the Funds with the cash flow of a given PPP project. Co-financing of a PPP project under the Funds influences the amount of regular payments by the public sector and also the structure and costs of project funding and their structure.

In the case of a PPP project supported from the Funds, the contracting authority aims at reducing the overall volume of payments to a private investor during the PPP project duration. Such payment volume decrease is possible thanks to payment of some project investment costs by means of grants from the Funds and related reduction of financing costs of some investment costs paid by a private investor. As regards PPP projects, the investment costs of the private entity affect the amount of regular payments of the public sector.

There are two basic models describing the impacts of co-financing under the Funds on the payments by the public sector to the private sector:

1. **Decreased regular payments of the public sector:** proportional decrease of regular payments by the public sector to a private entity for the entire project life cycle by an amount of costs already paid from the Funds during the preparatory and investment phases.
2. **Deferred payments of the public sector:** The public sector may be interested in deferred start of regular payments until future. Regular payments remain in the same amount as if co-financing of a PPP project under the Funds did not take place. The period for which the payments are deferred depends on the volume of co-financing under the Funds.

Practical feasibility of both above-mentioned models depends especially on the contractual agreement between the public sector and a private investor. In practice we may imagine also the combination of both aforementioned approaches.

Options to draw contributions from the Funds:

1. **Use of contributions from the Funds after completion of the project investment phase.** Ex-post payment of a contribution after control of eligible expenditure incurred during the project investment phase.
2. **Use of contributions from the Funds already during the project investment phase.** In this option the grant is drawn after completion of individual project phases such as in the case of standard projects supported from the Funds. The public entity starts paying the private investor already during the investment phase of the project. In this event the PPP principle “no service,

no payment” may be infringed; therefore the private entity must be sufficiently motivated to complete the project. In the case of some projects with an investment phase exceeding three years there is a risk that a partial share from the annual allocation may be lost, which, given the size of PPP projects, is not a negligible issue. This issue could be resolved if a special holding fund was established where the drawn money would be accumulated and gradually paid to a private investor during the project life. Under the current legislative conditions there is no Model 5: Holding Fund.

3. **Restrictive condition of ESC:** The public entity in the role of a beneficiary must directly cover 100% of project eligible expenditure which will be reported in the form of a payment claim together with cleared invoices to the managing authority. An issue appears if the beneficiary is a public entity, but the investment phase is implemented from the private investor’s resources (for a detailed description of the issue and possible solutions see chapter 5 – Model 3: Public Beneficiary).
4. **Invoice maturity deferral system** will mean that the project investment costs will be paid no sooner than during the operational phase. The invoices will be due within three to four years after completion of the project investment phase in such a way so that they would be paid and submitted to the managing authority by the end of the programming period. The proposed solution has the following disadvantages:
  - artificial prolongation of the project duration;
  - on-going submission of payment claims until 2015;
  - the managing authority must thoroughly plan drawing on the Funds in individual annual allocations.

The specific amount of grant from the EU fund and its timing may not be known in all the cases when a PPP project is combined with the Funds at the time of signing the PPP project contractual documentation between the public sector and a private investor. It means that in the project business case there may be a certain degree of uncertainty regarding the volume of the future cash flow. Assessment and allocation of risks related to the potential deviations from the amount and timing of grants from the Funds must be taken into account in a detailed feasibility study generated at the beginning of the PPP project and especially in the contractual documentation of a PPP project made between the public sector and a private investor.

*In the case of some projects the relatively complicated combination of cash flow of a PPP project co-financed under the Funds may cause certain uncertainty regarding timing and amount of grant used at the moment of signing the contractual documentation with a private investor. On-going drawing on the Funds during the project investment phase after achievement of milestones set in advance contradicts the PPP principle according to which the public sector starts paying only after hand-over of infrastructure/service for use.*

### 3.2.2 Revenue-generating Projects

According to the current interpretation of the Commission (Information notes 58 and 64) the PPP projects are *de facto* automatically included in the group of revenue-generating projects. In the case of revenue-generating projects the share from the Funds is decreased by the current value of net income from investment during a specific reference period and the eligible expenditure is co-financed under the Funds only up to the amount of the financial gap (i.e. the difference between the current value of project costs and revenues).

Article 54 Paragraph 4 “General Provision” provides a detailed specification of projects generating revenues. From the context of this article, it is implied that projects under state aid rules are excluded

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from projects generating revenues. This means that the private entity, as a beneficiary, must be in compliance with the rules of the Regional Map of State Aid granting the subsidy in the full amount of 40 percent of eligible expenditure, not only in the amount of the calculated financial gap.

Furthermore, for the programming period 2007-2013 the maximum possible support is defined as a fixed part (in %) of the financial gap (see 2.1.2.2) specific for each type of the Fund (e.g. limiting of the maximum rate of financing of 85% for the Cohesion Fund and ERDF). Because of these rules the support awarded to the revenue-generating projects is considerably decreased.

In this case the barrier is not only reduction of support for individual funds, but also the definition of revenue-generating projects (i.e. its interpretation) within the framework of the rules being prepared for the new programming period 2007-2013. The definition of revenue-generating projects may be construed in such a way that the revenue-generating projects automatically include not only the projects which generate real income from direct payments from infrastructure or service users (real toll), but also the projects which generate income from the shadow toll or fees for infrastructure/service availability paid by the Government to a private investor. If the rate of financing is reduced (e.g. in the amount of 85%), the Government must cover the maximum eligible expenditure, i.e. the financial gap up to the amount of 100% from the national co-financing sources (i.e. 15% in this specific case).

The above construction of the definition results in reduction of support for PPP projects from the Funds and increase of the national co-financing rate. During preparation of the programming period we recommend to communicate with the Commission as regards the change of interpretation which automatically categorises the PPP projects as a revenue-generating project, which leads to reduction of grants from the Funds.

Another important aspect is the duty to report sufficient revenue-generation by the project and return a proportional amount of the awarded grant to the EU budget. If over three years after completion of the operational programme some additional project revenue which was not included in calculation of the financial gap is identified, the awarded amount of grant will be proportionally reduced and returned to the EU budget pursuant to Article 54(4) of the draft General Regulation.

Nevertheless, the current wording of Article 54(4) does not explain when the operational programme is completed. It is obvious that completion of an operational programme may not be identical with completion of the programming period (the end of 2015), but there is no specific deadline by which the operational programme would be completed and the beneficiary would thus be obliged to report the additional revenue.

*Negotiations should be held with the Commission regarding inclusion of PPP projects in the group of revenue-generating projects and the precise construction of Article 54(4) of the General Regulation, who would be responsible for returning of the respective amount to the EU budget and how to proceed in such a case. Technical workshops with DG Regio and meetings of representatives of the Visegrad Countries should be used for communication with the Commission.*

*Communication with representatives of the Ministry of Finance has revealed that the obligations defined in Article 54(4) must be taken into consideration in the concession agreement, including the obligations to return a proportional amount of grants from the Funds to the EU budget for the period of three years after completion of an operational programme if revenue from investment is not included in calculation of a financial gap.*

### 3.2.3 Beneficiaries of Grants

If the beneficiary of a grant to a project financed under the Funds is characterised as an undertaking,<sup>53</sup> it is necessary to adhere to the state aid rules. The state aid rules are reflected in decrease of a ceiling which may be provided from public funds. The precise amount of these ceilings is set either in the Regional Map of State Aid Intensity or ensues from the block exceptions set for specific sectors. Generally speaking, the awarded amount of grants from the Funds amounts to the maximum value of 40% of total eligible expenditure in the case of undertakings as beneficiaries as proposed by the Regional Map of State Aid Intensity.

Based on the aforementioned facts, as regards beneficiaries we prefer an entity which does not meet the criteria of an undertaking<sup>54</sup> and is eligible for a bigger amount of grants from the Funds.

### 3.2.4 Restrictions on Expenditure Eligible for Financing under SF

If a PPP project is to be financed using grants from the Funds, first of all it will be necessary to clearly specify which phases and what types of costs will be eligible for financing under the Funds. PPP projects plan the involvement of a public entity in the following stages:

- **preparatory** – aiming at drawing up the tender documentation, implementation of the tender and selection of the supplier of works/services;
- **investment** – acquisition of investment, e.g. building infrastructure, construction of a building;
- **operational** – rendering of public services.

If we consider use of financing under the Funds in all three project phases, we face complications relating to the fact that the period of duration of the concession agreement is longer than the seven-year programming period. Furthermore, the operational phase is identical with the project sustainability phase during which compliance with the project goal and the monitoring indicators binding on the beneficiary according to the decision to award a grant is controlled. During the sustainability phase, grants from the Funds are not drawn; on the contrary, the beneficiary may be asked to return a part of the subsidies in case there are discrepancies between the real status and the concluded contractual terms (e.g. the constructed facility is not used for non-profit activities, but for commercial purposes).

Given the said facts, we recommend to concentrate grants from the Funds especially on payment of costs incurred during the preparatory and investment phases.

#### Definition of eligible/non-eligible expenditure

The Commission regulations define selected groups of expenditure which cannot be financed under the Funds (see 2.1.2.3). At the national level, both eligible and non-eligible expenditure is defined in a greater detail. As regards PPP projects, it is necessary to resolve the issue of eligibility of expenditure in the area of acquisition and lease of buildings and land, acquisition of additional tangible and intangible fixed assets, some operating costs, VAT, etc.

#### Payment of costs of project documentation

PPP projects are demanding already in the project preparatory phase in terms of time, administration and costs. During the project preparatory phase these are costs incurred before the start of project

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<sup>53</sup> For the sake of simplicity the term “private entity” is used in the below section.

<sup>54</sup> For the sake of simplicity the term “public entity” is used in the below section.

implementation. Under the current conditions the costs of project documentation are defined either as non-eligible expenditure or a percentage limit from the maximum amount of eligible expenditure is determined (e.g. in the amount of 5% in the case of the SPD Objective 2 and JROP programmes). As for PPP projects, based on our to-date experience, the preparatory phase is even more demanding, therefore we recommend to take consideration of increase of the percentage limit from the total amount of eligible expenditure. Also, the financial intensity of preparation of PPP projects co-financed under the Funds could be, to a large extent, cushioned if the costs for preparation of such a project could be paid from the technical assistance funds. The Commission also supports the proposed solution and recommends including the costs of preparation of PPP projects in technical assistance. To that end it would be desirable to make sure that the existing wording of Article 44 of the General Regulation would make such a procedure possible or to straight away provide for amendment to Article 44 so as to allow for the same as Article 43(1) with respect to the Commission, i.e. financing of preparation of a specific “project”.

#### Jaspers initiative

Another option is to use the Jaspers initiative for major projects (see chapters 2.1.1.4 and 2.1.1.5). This initiative focuses on provision of free counselling as regards preparation of project documentation of major projects from the stage of drafting the letter of intent up to the phase when it is submitted for approval to the Commission.

### 3.2.5 Project Profitability

If PPP projects are co-financed under the Funds, it may give rise to the sensitive issue of extremely high profit of a private entity<sup>55</sup> during the project. It may result from the market conditions, but also, e.g. from a low-quality feasibility study, low-quality contractual documentation, information asymmetry, lack of experience of the public entity, etc.

The Commission does not define the admissible amount of project profitability. Fiche No. 64 defines the indicative internal revenue rate for selected sectors. On the other hand, the Fiche allows for exceeding of the internal revenue rate in well-grounded cases. Nevertheless, the Fiche does not explain under which conditions the internal revenue rate may be increased and which entity is authorised to make such a decision (the managing authority or the Commission).

The said risk may be mitigated to a certain degree already at the beginning of the project by producing a detailed feasibility study (Outline Business Case). This study assesses cost-efficiency of the PPP alternative of project solution and the alternative to provide grants from the Funds with respect to the project profitability.

Assessment of cost-efficiency of the PPP alternative to resolve a specific project is based on comparison of financial flows of the basic alternative (standard public contract, calculation of PSC –

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<sup>55</sup> The methodology of evaluation of a specific project profitability from the point of view of the Commission is contained in the “Guide to Cost-benefit Analysis of Investment Projects”. Fiche 58 also deals with the assessment of project profitability. It reads that the expected profitability rate expressed by an internal revenue rate should correspond with the level of risk relating to investment acquisition, its financing and putting into operation. External risks such as the national economic situation should be taken into consideration, too. Another important aspect is delineation of the expected period of return on investment (e.g. in the case of the manufacturing sector the period of time of return on investment is estimated at 10 years, in the case of environmental infrastructure it equals 20-30 years). The model of an adequate profitability rate may be also applied in the same way to the PPP model co-financed under the Funds. Compliance with a transparent procedure when investment will be operated by a private investor selected on the basis of a tender remains a binding condition. Fiche 58 also does not provide comprehensive information and refers to another Commission statutory instrument, which will define the benchmarks and procedures for specifying the internal revenue rate depending on the nature of investment.

public sector comparator) and the PPP alternative and comparison of risks relating to both the alternatives as well as calculation of the value for money.

Cost-efficiency of the PPP option of project implementation is determined especially by the following factors:

- assumed value for money;
- qualitative aspects of the PPP alternative, including the implementation extent and form;
- risks related to the individual alternatives of project implementation;
- the most advantageous allocation of risks between the public sector and a private entity;
- expected cash flow for the entire project life cycle;
- financial affordability of the PPP project alternative for the public sector;
- selected payment mechanism;
- selected strategy to achieve optimum contractual solution of the project (optimum project structure).

### 3.2.6 Incorrect Choice of the PPP Type for a Specific SF Project

We face a risk that the chosen type of the PPP project will not meet the conditions of the respective operational programme and the rules for use of SF (e.g. limits in the area of infrastructure ownership by a private investor). Another risky point is building and/or fulfilling of the roles and responsibilities of the individual entities in the implementation structure while meeting the conditions of PPP projects. It is closely related to recruitment of personnel for the implementation structures for administration of PPP projects.

Given the uniqueness of PPP projects, it is usually impossible to use a universal implementation structure and procedures in the same way as the programme and project operations are set within the Funds. Because of this it is necessary to evaluate individual types of PPP projects in relation to the relevant operational programme and the planned project. Given the EU rules, the individual types of PPP (e.g. BOT, DBFO, etc. – see Annex No. 1) have strengths and weaknesses which must be taken into consideration from the beginning of the PPP project. The most suitable form for a specific project must be chosen based on these strengths and weaknesses. It is particularly vital to take account of the specific nature of contractual terms in relation to the nature of the project, e.g. rendering of services, operation contracts, lease contracts. It would be important to assess the said risk in terms of the ESC rules before proposing a specific structure of a PPP project.

*First of all, application of the PPP model to the respective programmes should be evaluated given the capability and capacity of the public sector to implement PPP projects and benefit from them. Evaluation of a PPP model suitability is closely linked to the interest of the private sector to implement PPP projects and benefit from them.*

*The choice of a specific type of the PPP model is further analysed within phase II of the Project in relation to the model combination of a PPP project with co-financing under the Funds.*

## 3.3 Organisational and Process Barriers

### 3.3.1 Absorption Capacity

When selecting suitable priorities for application of a PPP model co-financed under the Funds in the framework of individual operational programmes, we cannot base the selection only on the focus and list of supported activities. It may happen that a suitable fund is found, but an insufficient amount of

funds would be allocated to the respective measure. A specific example may be given in the case of the ROP programmes where allocation of funds amounts to some CZK 1.5bn a year per one cohesion region. Out of this annual allocation approximately CZK 100M may be earmarked for a PPP project. The remaining funds must be divided among other priorities under a given ROP.

On the basis of the aforementioned facts it is necessary to select suitable measures which would satisfy the conditions for PPP projects in terms of their nature and financial volume

### **3.3.2 Control Mechanisms and Monitoring**

At present we cannot objectively evaluate legislation regarding control mechanisms and monitoring in a PPP model as a concession agreement pursuant to the concession law has not been concluded in the Czech Republic yet. Nevertheless, based on the to-date experience, in the case of PPP projects, control takes place at the moment of hand-over of investment for use and further during operation on the basis of pre-defined performance parameters and control mechanisms. The control and performance measurement system is defined by the contractual documentation (concession agreement) concluded between a public entity (contracting authority) and a private investor. This system must be designed so as to motivate the private investor to remedy the issues related to non-compliance with the set performance parameters, including availability of a service in a given period. On the other hand, in the case of projects financed under the Funds, the control procedures have been standardised and are implemented either upon completion of the project phase when the beneficiary submits a payment claim or after a set period elapses (the supported beneficiary must submit a monitoring report at least once every six months).

The control and performance measurement system applied to PPP is closely related to the payment mechanism based on which payments will go to a private supplier for the entire period of project duration. Throughout the project duration the mechanism must be functional in order to motivate the operator to provide the required services and at the same time to retain an optimum value for money and desirable risk allocation.

However, the control mechanisms may not be considered a limiting barrier which would prevent implementation of PPP projects co-financed under the Funds. The said facts must be, nevertheless, taken into account when drafting the concession agreement. It must incorporate the binding terms ensuing from the relevant Commission regulations and related operational programmes. Beneficiaries for subsidies from the Funds agree to abide by these conditions in the decision to award a grant.

We must take into consideration that preparation of on-going and final monitoring reports and due application of control procedures (both administrative as well as on-the-spot checks) will require the private investor to supply all necessary information and accounting documents. Furthermore, we must address the issue which information on a private investor would be recorded in the monitoring system and in which way to enable the control entity to access the facility and seat of a private investor.

Authorisation of Czech inspectors is stipulated especially by the Act on Financial Audit (320/2001 Coll.) and applies to anybody applying for or receiving a grant. If the requested or proposed control entity structure includes the entities which do not have control powers, either the control entity system must be re-valued or legislation must be amended (the first solution seems to be easier if it does not hinder system effectiveness to a larger degree). At the same time, it should be provided for the following situation within a project: if there is an entity which is to be controlled, but does not fall into the beneficiary category, it is necessary to have contracts obliging such entities to submit to controls and governing strategic partner's responsibility for such entities as well as fulfilment of such obligation.

### 3.3.3 Risks Relating to Project Implementation Timing

PPP are long-term projects entered into for a period of 25 and more years. Consequently, they considerably exceed the programming period of the ESC policy. The ESC policy is based on a seven-year programming period and the annual allocation of the respective operational programme may be drawn and accounted for the period of the following three years/two years in compliance with the N+3 rule (starting from 2011 the N+2 rule will be applied). It is the managing authority or the paying authority, not an beneficiary drawing on the Funds that is responsible for compliance with the N+3 or N+2 rule. Currently the period of duration of SF projects equals some 24 months and is prolonged up to the period of 30 months in the selected measures. Under optimum circumstances, the project implementation could take up to 7.5 years (the project must be completed approximately in July so that there would be enough time for accounting for costs in relation to the Commission). In such a case funds for the first project phase would be paid from the 2007 allocation, for the second phase from the 2008 allocation, etc. The said model puts a greater emphasis on the monitoring system and control of drawing on funds.

Another important aspect pertains to the different procedures in the PPP model and the projects co-financed under the Funds. Let's take a good example: it is the phase when the tender for supplier of works/services takes place. In the case of projects financed from the Funds, the tender is usually held after awarding of a grant. The beneficiary adopts this approach because the costs paid for legal services related to preparation of tender documentation may be included in eligible expenditure. Such a procedure has a drawback and that is defining of technical parameters, the timetable of activities or total investment costs directly in the project application and the said data are binding as regards issuance of the decision to award a grant. If the supported beneficiary wanted to make additional amendments to the financing contract in relation to the offer of works/services provided by the supplier, the scope of any changes is rather narrow and also requires approval by the managing authority. OP Industry and Enterprise, e.g. accepts only the following changes in conditions of awarding a grant:

- **change in the phase deadline** (if it exceeds four months, it must be approved by the managing authority);
- **change in the amount of costs** (additional approval is necessary also for increase of one of the budgetary items by 20% with the same budget volume; other budgetary item(s) must be automatically decreased by a proportional amount).

Another open issue pertains to determination of the starting point when to assess eligibility of expenditure. Pursuant to Article 55(1) of the General Regulation the group of eligible expenditure includes such costs that were incurred since the day of submission of the operational programme or starting from 1 January, 2007.

The available volume of funds is derived from the approach of the managing authorities to the following issues:

- **setting of the system of calls for proposals** – system of several rounds of calls or on-going calls;
- **approach to drawing on funds** – acceptance of projects for an annual allocation or acceptance of projects for the entire allocation of the programming period (2007-2013).

## 3.4 Other Barriers

### 3.4.1 Political Restrictions

The relevant resolution governing preparation of public administration entities for the new programming period (e.g. Government Resolution No. 245/2005) does not mention application of PPP models with use of the Funds and does not define priority areas in which the PPP model may be applied. If application of the PPP model is not stipulated by a binding statute, such as Government resolution, the estimated development may lead to the following complications:

- **setting of varying conditions** for application of PPP projects at the level of individual ministries;
- **setting of varying procedures** relating to preparation and subsequent implementation of PPP projects;
- **insufficient linkage to the priority objectives of the national strategies** (e.g. Economic Growth Strategy of the Czech Republic) and related fragmentation of financial allocations to smaller projects.

### 3.4.2 Insufficient Interest of the Private Sector

Our experience abroad is that major projects using the PPP model are interesting for the private sector. If tender conditions are set well and trust is gained, any fear of lack of interest on the side of the private sector is irrelevant. The regions may be slightly sceptical. Therefore, it is paramount to set clear rules as regards project costs, operating revenue, project timetable, ownership relations, assignment of duties between the private and public sector so as to sufficiently motivate the private investor to implement the project. In this respect a good-quality and qualified awareness campaign addressing the private sector is vital.

## 4 Areas Proposed for Combining PPP and EU Funding by Individual Operational Programmes

Areas (model projects) considered suitable for combining PPP and the EU funding are based mainly on the analysis of selected reference projects implemented in selected EU countries. Apart from know-how of the consortium of authors, suitable PPP projects have been identified based on meetings with representatives of the below stated government authorities who provided valuable information on their plans within their ministries.

- Combined PPP and EU funding seems to be most efficient if used for large infrastructure projects, in particular in the fields of transport and the environment (investment cost > CZK 1bn).
- Although operational programmes (Transport, Environment, Business and Innovation, and Competitiveness) seem to be the most suitable for a combined PPP and EU funding under current conditions, this type of funding may be also effective for other OPs, if there are suitable projects.
- Regional OPs represent a separate category – in theory, implementation of certain major projects is possible.
- Selection of the most suitable model depends, to a great degree, on a specific project; the table below lists models suitable for implementation of model projects. Generally speaking, all presented models can be *de facto* used for selected OPs (with the exception of Model 5).

Table summarizing the most suitable model projects combining PPP and EU funding:

OP	Model Projects	Commentary on State Aid	Convenient Model of PPP and EU Funding
<b>Transport (MoT)</b>	<ul style="list-style-type: none"> <li>• Motorway and road infrastructure</li> <li>• Railway infrastructure</li> <li>• Airport development</li> <li>• Other transport structures – bridges, tunnels, etc.</li> <li>• Modernisation of waterways</li> </ul>	<p>Relatively low risk (infrastructure owned by the Czech Republic)</p> <p>Separate assessment required for airports and ports (possibility of combined private ownership, land transfers, etc.)</p>	<p>Model 1 Model 2 Model 3</p>
<b>Environment (MoE)</b>	<ul style="list-style-type: none"> <li>• Water supply and sewerage</li> <li>• Waste water treatment plants</li> <li>• Waste management (e.g. incineration plants)</li> <li>• Elimination of environmental burdens</li> <li>• Renewable resources</li> </ul>	<p>Separate assessment required (possibility of combined private ownership, land and infrastructure transfers, etc.)</p>	<p>Model 2 Model 3</p>
<b>Prague (Prague City Council)</b>	<ul style="list-style-type: none"> <li>• Metro construction</li> <li>• Prague ring road</li> <li>• Water supply and sewerage</li> </ul>	<p>Separate assessment required (possibility of combined private ownership, land and infrastructure transfers, etc.)</p>	<p>Model 1 Model 2 Model 3</p>
<b>Business and innovation (MIT)</b>	<ul style="list-style-type: none"> <li>• Brownfield regeneration</li> </ul>	<p>Relatively high risk – separate assessment required (also in terms of state aid beneficiaries)</p>	<p>Model 1 Model 4</p>

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The table below does not present an exhaustive list of options, but just a sample in which areas the PPP principle could be theoretically applied. It is expected that the table is going to be further detailed and expanded during the preparation for the programming period 2007-2013.

<b>OP</b>	<b>Priorities</b>	<b>Suitable PPP Projects</b>
Transport (MoT)	Development of transport infrastructure of the TEN-T network, including aspects of security, interoperability and environmental impact and development of further railway infrastructure with a clear environmentally friendly impact – CF	<ul style="list-style-type: none"> <li>• Motorway and road infrastructure</li> <li>• Railway infrastructure</li> <li>• Airport development</li> <li>• Other transport structures – bridges, tunnels, etc.</li> <li>• Modernisation of waterways</li> </ul>
	Development of connecting networks of road infrastructure and support of multimodal cargo transport in order to protect the environment	
	Capital City of Prague – development of important transport links – CF	
Environment (MoE)	Protection of water and air, sustainable use of natural resources	<ul style="list-style-type: none"> <li>• Water supply and sewerage</li> <li>• Waste water treatment plants</li> <li>• Waste management (e.g. incineration plants)</li> <li>• Elimination of environmental burdens</li> <li>• Renewable resources</li> </ul>
	Industrial pollution and waste management	
	Nature and landscape, education	
IOP	Efficiency, quality and capacity of public administration	<ul style="list-style-type: none"> <li>• Infrastructure and services related to integration of information and emergency systems</li> <li>• Health care facilities – infrastructure and support services</li> <li>• Development concept of digital broadcasting in the Czech Republic</li> <li>• Information infrastructure</li> </ul>
	Information society development	
	Development of tourism	
	Use of the cultural potential	
	Sustainable urban development	
Business and Innovation (MIT)	Business and innovation	<ul style="list-style-type: none"> <li>• Brownfields</li> </ul>
	Business and innovation environment	
	Services for business development	
Research and Development for Innovation (Ministry of Education, Youth and Sports)	Fostering R&D capacities and their integration to the European Research Area (ERA)	<ul style="list-style-type: none"> <li>• Campuses</li> <li>• Business incubators</li> </ul> <p>Specific projects:</p> <ul style="list-style-type: none"> <li>• University campus in Ústí nad Labem</li> <li>• Educational centre in Terezín</li> </ul>
	Co-operation of the public sector with the private sector in R&D for innovation	
Education (Ministry of Education, Youth and Sports)	Modernisation of educational systems of elementary and secondary schools, including technical colleges	<ul style="list-style-type: none"> <li>• Major educational programmes</li> </ul>
	Modernisation of tertiary education including preparation of human resources for R&D	
	Development and support of further education	

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Human Resources and Employment (MoLSA)	Adaptability	<ul style="list-style-type: none"> <li>• Major educational projects</li> <li>• Co-operation in the education of public administration</li> </ul>
	Active policies of the labour market	
	Social integration and equal opportunities	
	Public administration	
	International co-operation	
ROP Southwest	Accessibility of centres	<ul style="list-style-type: none"> <li>• No project above CZK 100M has been identified</li> </ul>
	Stabilization and development of settlements	
ROP Southeast	Development of transport and information infrastructure	<ul style="list-style-type: none"> <li>• No project above CZK 100M has been identified</li> </ul>
	Supporting regional development and prosperity	
ROP Central Moravia	Transport	<ul style="list-style-type: none"> <li>• No project above CZK 100M has been identified</li> </ul>
	Integrated regional development and renewal	
	Tourism	
	Quality of life	
ROP Northwest	Urban regeneration and development	<ul style="list-style-type: none"> <li>• Transport</li> <li>• Transport services</li> <li>• Indirect business support (Brownfields)</li> </ul>
	Integrated support of regional development	
	Accessibility and transport services	
	Sustainable development of tourism	
ROP Northeast	Development of transport infrastructure	<ul style="list-style-type: none"> <li>• No project above CZK 100M has been identified</li> </ul>
	Development of urban and rural areas	
	Tourism	
	Business and innovation development	
ROP Moravia-Silesia	Regional infrastructure and accessibility	<ul style="list-style-type: none"> <li>• No project above CZK 100M has been identified</li> </ul>
	Regional business support	
	Development of urban and rural environment	
ROP Central Bohemia	Transport	<ul style="list-style-type: none"> <li>• Regional airport development</li> </ul>
	Tourism	
	Quality of life in the region	
	Absorption capacity	
Technical Assistance		<ul style="list-style-type: none"> <li>• Preparation of model PPP projects</li> <li>• Drafting of external reports on PPP projects</li> <li>• External control over implementation of PPP projects</li> <li>• Drafting of a study for contracting authorities of PPP projects defining the roles and tasks of the PPP project contracting authority</li> <li>• Fostering expertise of public administration staff dealing with PPP projects</li> </ul>

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OP Prague – Adaptability	Development of knowledge economy	<ul style="list-style-type: none"> <li>• Major educational projects</li> </ul>
	Supporting entrants to the labour market	
	Development of life-long learning	
OP Prague – Competitiveness	Infrastructure and accessibility	<ul style="list-style-type: none"> <li>• Metro construction</li> <li>• Prague ring road</li> <li>• Water supply and sewerage</li> </ul>
	Innovation and businesses	

## **5 Basic Models Combining PPP and EU Funding**

The following chapter summarises the basic models combining PPP and the EU funding. As regards the below-listed models, under the current conditions the “Public Beneficiary Model” and the “Public Co-financing Model” seem to be the most realistic and practical. Implementation of the “Co-financing-by-Operator Model” could also have big advantages. For your information, we also present the “Holding Fund Model” which cannot be implemented in practice here due to the existing EU rules and the Czech legislation. Please notice that there may be several sub-versions in the framework of each model, depending on the specific project conditions, possibility to achieve the maximum value for money and private sector’s willingness to participate in a given project. For the sake of simplicity the Government has been chosen as a contracting authority here.

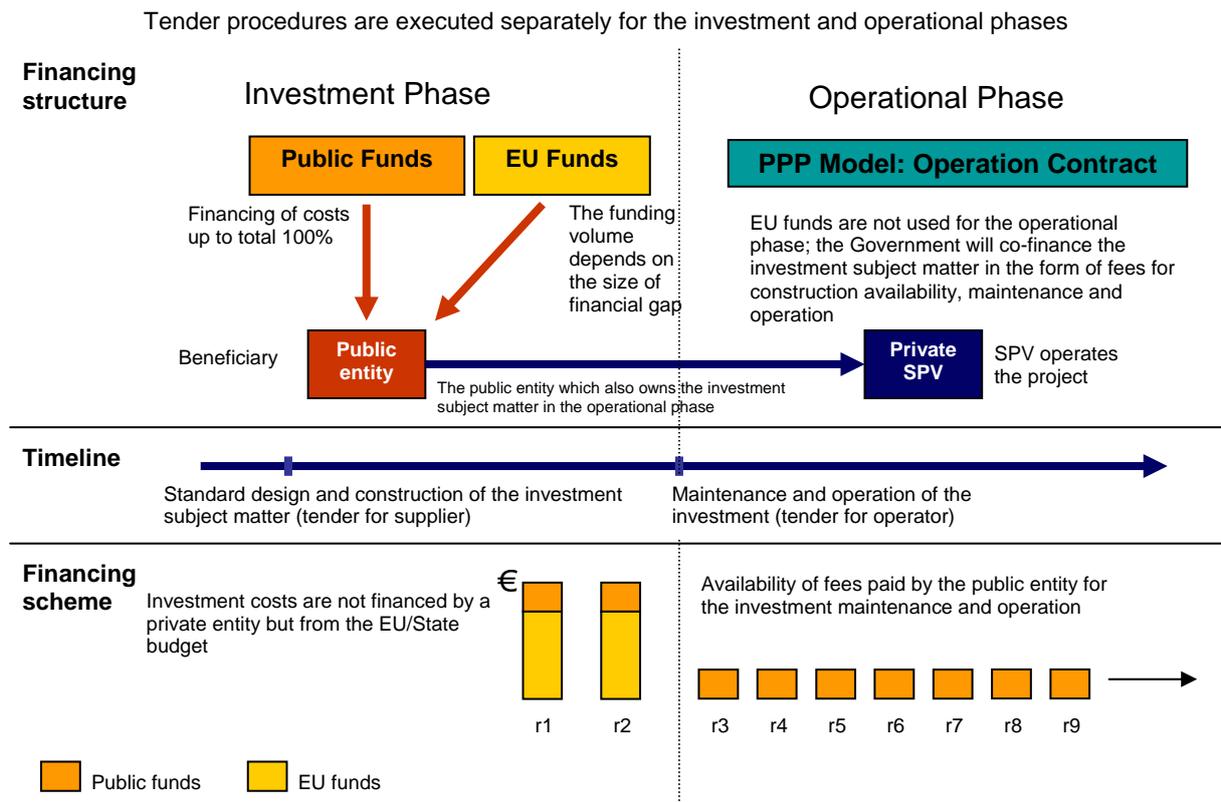
### **5.1 Models with Separated Investment and Operational Phases**

The models presume that implementation of the investment and operational phases are separated in such projects where separate public procurement/concession procedure is used (however, these procedures may be merged, too). The investment phase takes the form of a standard tender for supplier of infrastructure and is co-financed under the Funds. In the case of these models, the operational phase is implemented using a PPP project. In this context a tender for a private operator and maintainer of infrastructure throughout the entire project life cycle (usually 20-40 years) is invited. In some specific cases a tender for the operational phase may precede the tender for the investment phase (see e.g. the current practice in the case of waste water treatment plants).

### 5.1.1 Public Co-financing Model (Model 1)

The project investment phase is co-financed under the Funds (ideally, co-financing may amount to maximum of 85% of eligible expenditure – if the project is not classified as a revenue-generating project). If it is, the EU funding volume depends on the size of the financial gap calculated for a given project. The remaining costs above the grant from the EU funds are covered from the national resources and the beneficiary’s resources (e.g. if it is an institution receiving contributions from the state budget).

The project operational phase is based on a PPP model without drawing on the EU funds. The Government invites a tender for a private entity and pays the operational phase costs, i.e. the fees for infrastructure availability throughout the entire project life cycle.



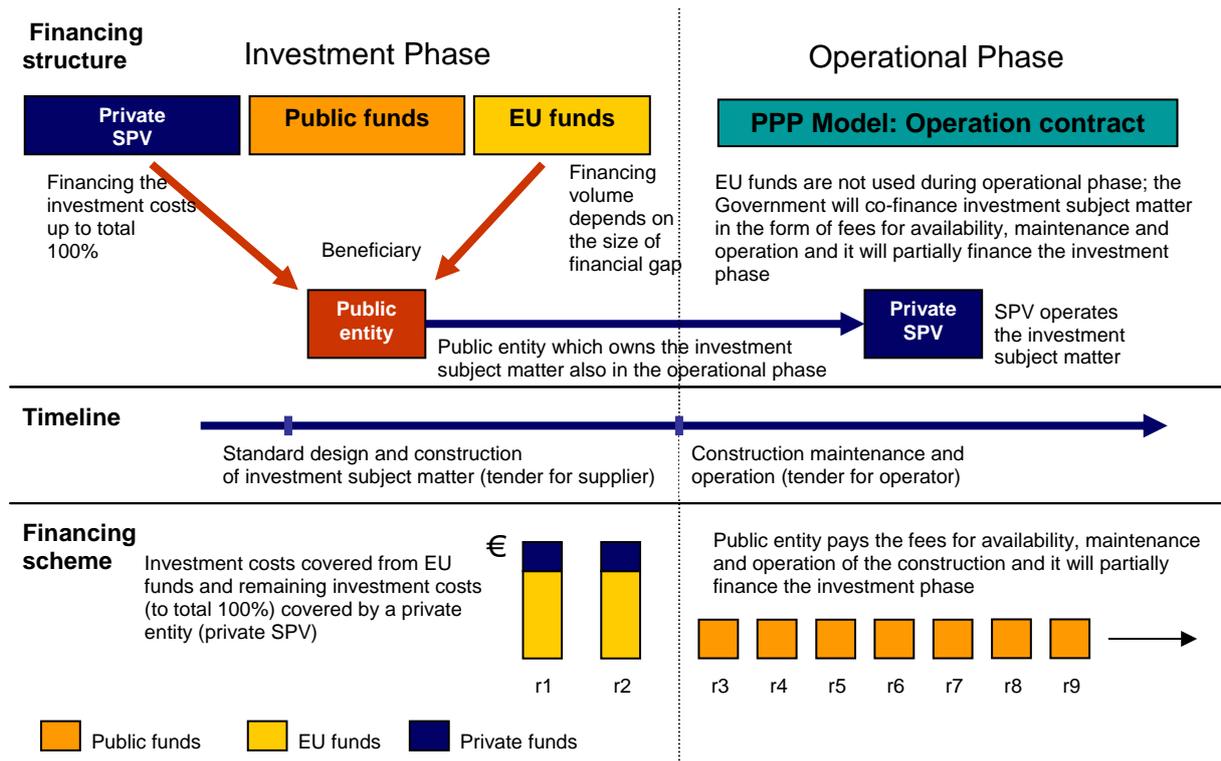
MODEL 1	
<b>Advantages</b>	<ul style="list-style-type: none"> <li>• Maximum contribution for PPP projects from EU funds is up to 85% of eligible costs of the financial gap;</li> <li>• More simple use of EU funding (procedures, fewer number of involved entities); and</li> <li>• Tender for operator will correspond with technical possibilities of infrastructure/investment subject matter.</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>• Beneficiary must ensure the financing of remaining project costs;</li> <li>• Additional costs of two tenders (investment and operational phases);</li> <li>• Higher operating costs (private operator does not have a chance to influence the project design); and</li> <li>• Limited possibilities of shifting risks to a private entity.</li> </ul>

### 5.1.2 Operator Co-financing Model (Model 2)

The project investment phase is co-financed under the Funds. The remaining costs of a grant from the EU funds are paid by a private investor (private entity) selected within the framework of a PPP project launched for the operational phase. The private investor is operating and maintaining the infrastructure for the entire project life cycle, while co-financing the project investment phase. The Government invites a tender for a private entity and covers the costs of the operational phase, including a part of costs of the investment phase in the form of fees for infrastructure availability for the entire project life cycle. From the point of view of public procurement procedure, the most suitable solution seems to be use of one public procurement procedure (the private investor would then be involved both in the investment and operational phases and, furthermore, would provide own resources for a part of the investment phase). In the case of separate procedures, in the public procurement procedure the private investor would offer their financial services, i.e. a loan to co-finance the investment phase.

The advantage of this model is involvement of the private sector also in financing of the project investment phase. In the case of separate public procurement procedures, the disadvantage will be the fact that the private investor will exercise smaller influence as regards the form of the investment phase and subsequently will be unable to influence the project design in a way providing for the maximum efficiency of long-term operation.

Tender procedures are executed separately for the investment and operational phases



MODEL 2	
<b>Advantages</b>	<ul style="list-style-type: none"> <li>• Maximum contribution for PPP projects from EU funds is up to 85% of eligible costs of the financial gap;</li> <li>• More simple use of EU funding (procedures, fewer number of involved entities);</li> <li>• Tender for operator will correspond with technical possibilities of infrastructure/investment subject matter;</li> </ul>

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	<ul style="list-style-type: none"><li>• Private entity will ensure the funding of remaining project costs (in the form of a supplier loan or interest-free loan).</li></ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"><li>• Beneficiary must ensure the financing of remaining project costs;</li><li>• Additional costs of two tenders (investment and operational phases);</li><li>• Higher operating costs (private operator does not have a chance to influence the project design); and</li><li>• Limited possibilities of shifting risks to a private entity.</li></ul>

## 5.2 Models Combining PPP and the EU Funding in One Project

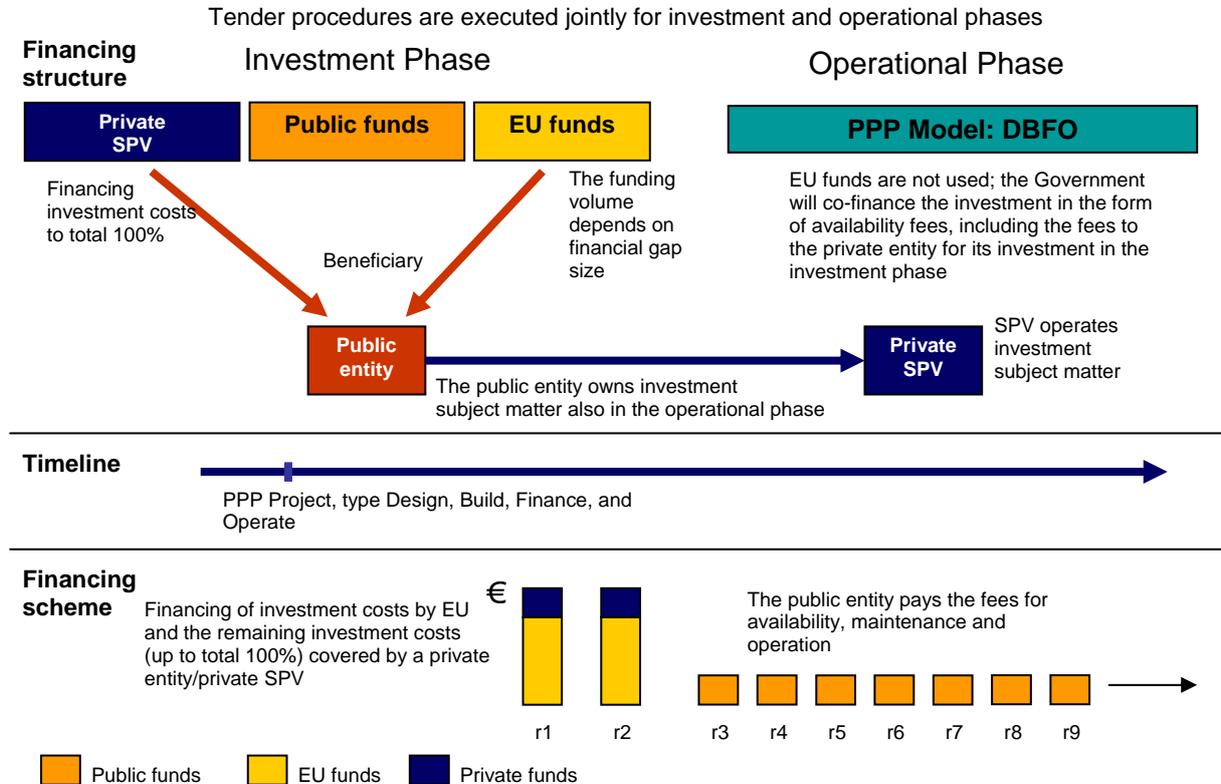
The models combining PPP and the EU funding in one project presume existence of a single tender for a private PPP investor – supplier both for the investment and operational phases. The rate of project co-financing under the Funds depends, among other things, on classification of the project as a “revenue-generating project” and the financial gap size in a given project.

### 5.2.1 Public Beneficiary Model (Model 3)

The public entity is a beneficiary and also a beneficiary of financial assistance under the Funds. At the same time, in both phases the public entity owns the infrastructure. The investment phase is financed under the Funds and the funds provided by the private entity in the form of an interest-free loan to the beneficiary. During the operational phase the private entity is only an operator of the subject matter (responsible for operation and maintenance of the subject matter) under a contract of lease made between the beneficiary as the lessor and the operator as the lessee.

The Government invites a tender for a private entity and covers the costs of both the investment (only the part financed from the private resources) and operational phases in the form of fees for infrastructure availability for the entire project life cycle.

In order to adhere to the PPP principle “no service, no payment”, it would probably be possible for the beneficiary to apply for a one-off grant after completion of the project investment phase. The said model may be applied provided that the project investment phase is finalised within the programming period. The other alternative rests with on-going drawing on the Funds after completion of individual project phases; nevertheless, the principle “no service, no payment” is then compromised.



MODEL 3	
<b>Advantages</b>	<ul style="list-style-type: none"> <li>• The maximum contribution from EU funds for PPP projects up to the limit of 85% of eligible costs of the financial gap;</li> <li>• Financing of investment costs by a private entity;</li> <li>• Using the advantages of the DBFO model*;</li> <li>• Motivation of the private entity for minimum overall project costs and performing all supplier services;</li> <li>• Lower operating costs of the project (the private operator may influence the project design); and</li> <li>• Greater chances of transferring risks to the private entity.</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>• Need to deal with the issue of paying investment costs by the beneficiary;</li> <li>• Under the current conditions, the structure of clearing the project costs is rather difficult because the operator (SPV) cannot pay the invoices directly to the supplier but needs to grant an interest-free loan to the beneficiary who pays supplier invoices.</li> </ul>

### 5.2.1.1 Model 3 – Restrictive Conditions of ESC Policy

According to the present rules, any public entity in the role of a beneficiary must directly cover 100% of the project eligible expenditure reported in the form of payment claims together with cleared invoices. If the beneficiary is a public entity, but the investment phase is funded by a private investor (Model 3: Public Beneficiary), it may give rise to an issue.

Possible solutions:

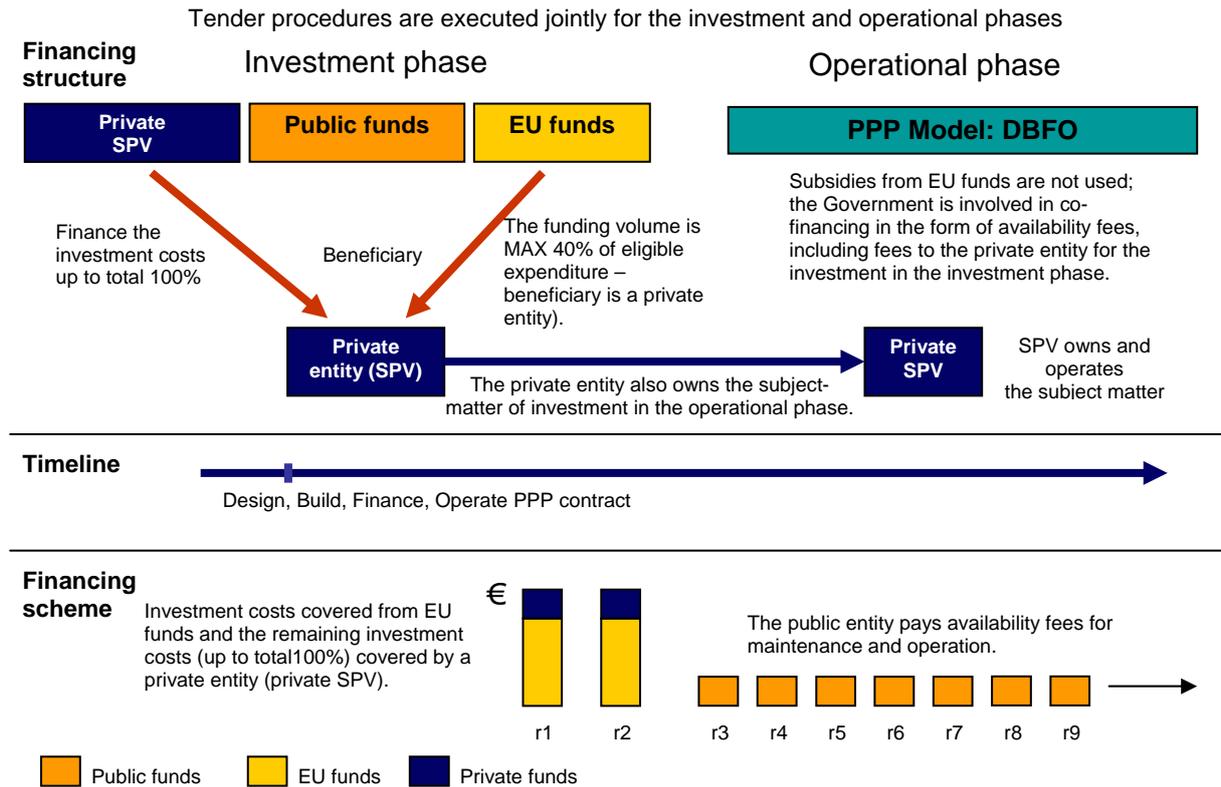
1. Consulting the Commission regarding the possibility to include the costs paid during implementation of the project by entity other than the beneficiary into the project eligible expenditure, while from the point of view of the beneficiary these would be future liabilities to be paid in the form of fees for availability in the operational phase.
2. Provision of an interest-free loan to the beneficiary by the private entity to be paid in the form of fees for services:
  - a. Provision of an interest-free loan to the beneficiary by the private entity to finance the eligible investment costs
  - b. Payment of the eligible investment costs by the beneficiary
  - c. Submission of payment claims by the beneficiary
  - d. Beneficiary’s receipt of a grant
  - e. Repayment of a part of the interest-free loan from the awarded grant
  - f. Long-term repayment of the remaining part in the form of fees for availability of infrastructure/service
3. Commercial loan

The disadvantage of loan-based solutions is a public debt increase for the period of project construction. In the case of an interest-free loan from a private supplier, the total project funding costs are likely to rise.

### 5.2.2 Private Beneficiary Model (Model 4)

The private beneficiary model is based on the fact that the private entity is a beneficiary and also a beneficiary of financing under the Funds. The private entity is selected by means of a tender for a private investor of a given PPP project. If the private entity is a beneficiary of financing under the Funds, it will be provided the maximum grant from the EU funds in the amount of 40% of the project eligible expenditure. The remaining part of investment costs above the grant from the EU funds is financed by a private entity.

The private entity owns infrastructure both during the investment and operational phases. Upon completion of the project operational phase, the infrastructure is transferred to the public sector.



MODEL 4	
<b>Advantages</b>	<ul style="list-style-type: none"> <li>• Financing of investment costs by a private entity;</li> <li>• Using the advantages of the DBFO model;</li> <li>• Motivating the private entity for minimum overall project costs and performing all supplier services;</li> <li>• Lower operating costs of the project (the private operator may influence the project design); and</li> <li>• Greater chances of transferring risk to a private entity.</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>• Minimum volume of received EU funds up to the limit of 40% of eligible costs of the financial gap; and</li> <li>• A limited number of priorities where a private entity may be a beneficiary.</li> </ul>

### 5.2.3 Holding Fund Model<sup>56</sup> (Model 5)

The Holding Fund Model represents an alternative where the private investor is building, financing and operating the infrastructure. The private investor is not financed directly from the EU funds as upon meeting certain EU rules, the support is drawn into the Holding Fund from which it is paid to the private investor gradually over the entire life cycle. This approach is in compliance with the PPP principle “no service, no payment” when the private investor is paid only upon putting the infrastructure into operation and handing it over to the public sector for use. For the Holding Fund to function well, there is one vital presupposition and that is to acknowledge the transfer of funds from the EU to the Holding Fund as drawing on funds so that the allocation would not be lost.

The Holding Fund could also be used for major investment projects with an investment phase exceeding three years endangered by the loss of an annual allocation or violation of the “no service, no payment” principle. This approach pertains especially to the major projects with the Government as a beneficiary (ministry, state agency, etc.) which has special annual allocations for the investment phase. Because of the likely application of the “no service, no payment” principle, there is a risk that an allocation would be lost.

The initial idea was to establish the Holding Fund at the Czech National Bank which would administer it and manage release of funds in co-operation with the Ministry of Finance of the Czech Republic. Nevertheless, practical implementation of the Holding Fund Model is not feasible in the CR due to the existing EU rules and the Czech legislation. In spite of that we consider this model the most suitable in terms of the PPP principles and national public funds.

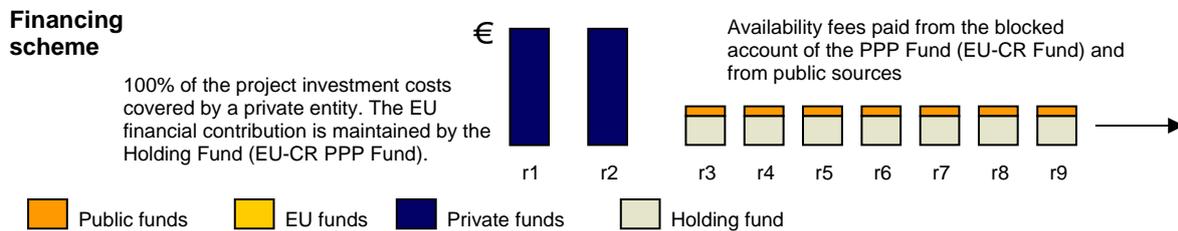
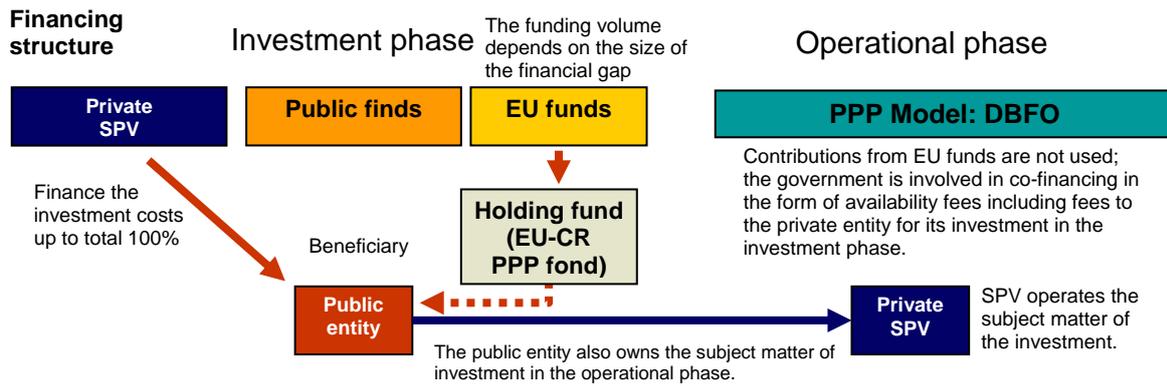
The figure describing functioning of the Holding Fund is based on Model 3; nevertheless, the Holding Fund principle may be used also in Model 4.

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<sup>56</sup> According to the representatives of the National Fund Department of the Ministry of Finance of the Czech Republic, this model is not feasible given the current legislative conditions.

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Tender procedures are executed jointly for the investment and operational phases



MODEL 5	
<b>Advantages</b>	<ul style="list-style-type: none"> <li>The maximum contribution from EU funds up to the limit of 85% of eligible costs of the financial gap;</li> <li>Compliance with PPP principles of projects (“no service, no payment”);</li> <li>Use of the advantages of the DBFO model;</li> <li>Motivation of the private entity for minimum overall project costs and performing all supplier services;</li> <li>Lower operating costs of the project (the private entity may influence the design of the project); and</li> <li>Greater chances of transferring risks to a private entity.</li> </ul>
<b>Disadvantages</b>	<ul style="list-style-type: none"> <li>Does not comply with the rules of the Economic and Social Cohesion under which EU funds must be used to cover investment costs; they cannot be used to create another fund from which financial means would be drawn as late as in the operational phase (even if used to cover investment costs); and</li> <li>The National Fund maintains that the Holding Fund Model is not currently feasible.</li> </ul>

#### 5.2.4 Basic Characteristics of Individual Models

	MODEL 1	MODEL 2	MODEL 3	MODEL 4	MODEL 5
<b>Number of tenders</b>	2	2 (1)	1	1	1
<b>Beneficiary</b>	PubE	PubE	PubE	PriE	PubE
<b>Financing volume from the EU funds</b>	Max. 85% of fin. gap	Max. 85% of fin. gap	Max. 85% of fin. gap	Max. 40% of eligible expend.	Max. 85% of fin. gap
<b>Co-financing entity</b>	PubE	PubE (PriE provides an interest-free loan)	PubE (PriE provides an interest-free loan)	PriE	PubE (PriE provides an interest-free loan)

Generally speaking, a financial analysis is recommended to be conducted for each project. The amount of the subsidy will be calculated in one of two ways:

- a) in the volume of 85 percent of the financial gap; or
- b) in the volume of 40 percent of eligible expenditure.

Based on results received on the financial analysis, if scenario “a” is more financially convenient, Model 3 “Public Beneficiary” should be applied where the volume of drawing from EU funds is maximised. Nevertheless, this model does not comply with one of the ESC policy rules defined in Article 66 of the General Regulation. It is a restrictive condition when the public entity as a beneficiary must directly pay 100% of the project eligible expenditure to be reported in the form of payment claims together with cleared invoices. The disadvantage of this rule is the fact that a private entity cannot take part in covering the remaining costs. However, if the rules cannot be changed at the Commission level, we recommend resolving the issue by the private entity’s providing funds to the beneficiary in the form of an interest-free loan which will be repaid gradually together with payment of fees for services.

From the viewpoint of infrastructure ownership, pursuant to Article 56 of the General Regulation, while the concession agreement is in force, the key factor is to adhere to the project objective and nature for the minimum period of five years after issuance of the decision to award a grant. In the case of PPP projects, this condition must be stipulated by the concession agreement.

In the case that the financial analysis results are more favourable in scenario “b”, we recommend applying Model 4 – “Private Beneficiary” except when the income from EU funds is maximised. In this model, there are no complications linked to the funding system in connection with the invoice submission for the controlling entity. The private entity, in this model, will have the role of a beneficiary directly authorised to submit payment forms together with paid invoices. It will also be possible to limit possible risks associated with the monitoring system, control system, and the submission of regular project progress reports. The private entity will be bound by all binding conditions.

## 6 Technical Assistance

The use of technical assistance (TA) in the new programming period is governed by Article 44 of the General Regulation. The wording of Article 44 suggests that the TA may be used to cover the following types of expenditure:

- Preparation;
- Management;
- Monitoring;
- Administration capacity building activities.
- Evaluation;
- Raising awareness;
- Control;

The CR intends to distribute the allocation amounting to 4% of the total allocation under the Convergence objective as follows: 2% shall be distributed among OPs and the remaining 2%<sup>57</sup> should be spent on a separate Operational Programme Technical Assistance (OP TA). The total allocation to OP TA amounts to CZK 17.6bn. (The total allocation means the Funds and national co-financing.)

### 6.1 Operational Programme Technical Assistance

Spending of funds from OP TA within the framework of PPP projects is deemed useful particularly in the following areas:

- Identification and preparation of model PPP projects co-financed under the Funds;
- Preparation of reports on PPP project implementation serving as source documents for meetings of the Monitoring Committee;
- External control over PPP project implementation (the advisor who provided counselling in the preparatory phase of the project may be given the preferential right to conduct controlling activities also in the investment and operational phases of the project);
- Preparation of studies for PPP contracting authorities (ministries, regions, municipalities, their organisations receiving contributions from the State budget or organisational units, etc.) to define tasks to be ensured by the PPP contracting authorities in all phases of a project implementation;
- Enhancement of the technical expertise of public administration officials involved in PPP project issues (initiation of investment projects, PPP project administration in all implementation phases).

#### Model projects

Interviews with officials representing individual ministries suggest that the model PPP projects should focus on the following areas in particular:

- OP Transport
- OP Environment (removal of environmental burdens, waste recycling, renewable resources)
- OP Business and Innovation (brownfields).

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<sup>57</sup> The 2% threshold for OP TA may be reduced for the benefit of ROPs.

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The current experience with the preparation of PPP projects in the CR suggests that the cost of a preparatory phase may vary from CZK 20M to 100M, depending on the technical intensity of a project.

Therefore, if we take into account the preparation of model projects in all the above specified areas, we need to ensure allocation from the TA in the approximate amount of CZK 450M. We recommend that the above allocation be reserved particularly for the beginning of the programming period to retain a sufficient time reserve for the subsequent project implementation.

Counselling related to the preparation of a model project:

Legal counselling	Legal due-diligence of the project
	Tender/concession procedure, bidding instructions
	Proposed contractual relationships of the PPP project
Financial counselling	Qualitative and quantitative analysis of alternative solutions
	Proposed way of securing the PPP project (scope of the project, proposed distribution of risks, project cash flow, payment mechanism)
	Strategy, type and time schedule of the tender for the selected alternative of the project implementation
Technical counselling	Technical due-diligence of the project
Services in the operational phase (if rendered within the programming period)	Control and preparation of monitoring reports

## **6.2 Technical Assistance within the Operational Programmes**

As for the drawing on TA, the draft OPs cover the topic in general terms only, and particularly in relation to the enhancement of activities related to the overall co-ordination of OPs. Article 44 of the General Regulation, however, refers to the funding of OP activities. Unfortunately, the term “activity” is used solely in relation to the TA and its definition is ambiguous. It is beyond any doubt, however, that the projects can be considered a specific form of implementation of the OPs and it can be concluded that the implementation of a project is an activity that forms inseparable part of an OP.

Within particular OPs an allocation amounting to 2% of the total eligible cost of a programme has been reserved for the TA priority. Specifically, the allocation for the TA varies between CZK 3,352M for OP Transport and OP Environment and CZK 1,059.6M for OP Research and Development for Innovation. Discussions with officials representing the managing authorities for OP Environment and OP Transport suggest that the financial allocation of the TA will be reserved to cover the cost of external evaluators of project applications and also the cost of external controllers entrusted with execution of on-the-spot checks. In addition to that, both ministries count upon installation of new software to regularly monitor the status of project implementation.

On the other hand, if we map the current status of drawing on TA funds, we come to the conclusion that for OP Infrastructure for the years 2004 and 2005 an allocation was earmarked in the amount of CZK 96.6M, of which the amount of CZK 45.9M, i.e. 47.5%, was allocated to projects as at 31/12/2005 (Source: Level of Drawing on the Structural Funds as at 31/12/2005). It can be drawn from this that part of the allocation could be earmarked for the building of the absorption capacity. Therefore, we recommend conducting an analysis that would stipulate the share of cost to provide external services, acquire a monitoring system, and enable enumeration of the financial reserve not covered by any specific projects so far.

OP Business and Enterprise extends the list of supported activities with additional activities focusing on administration capacity building. Therefore, as obvious from the above description, this priority can be used to fund seminars for public administration officials, which may also include PPP projects. The experience from the current programming period suggests that a part of the allocation will also be used to cover the cost of external evaluators and controllers. Nevertheless, as suggested by hitherto development, the amount earmarked for the TA in the years 2004 and 2005 amounted to CZK 177.4M and of this amount CZK 58.2M, i.e. approximately 33%, was allocated to projects as at 31/12/2005. (Source: Level of Drawing on the Structural Funds as at 31/12/2005). Therefore, we recommend to conduct an analysis similar to that of OP Environment and OP Transport and to check on the existence of a sufficient financial reserve that could be used to strengthen the absorption capacity.

In the case of OP Research and Development, the activities are defined pursuant to Article 44 of the General Regulation. In this case we recommend that the list of supported activities be extended with the absorption capacity building in order to prepare model projects, including those implemented under the PPP regime.

### 6.3 ROPs

An allocation for the TA priority per one ROP represents the amount of CZK 450M-638M; the annual allocation thus represents the amount of CZK 64M. Data from the MSSF Central suggest that the average drawn allocation amounts to approximately CZK 50M, and thus the above threshold can be considered appropriate to ensure due implementation of the ROPs and to cover cost of project evaluation and control, maintenance of the monitoring system, organisation of meetings of the implementing bodies as well as public seminars, development of evaluation projects mapping the results achieved within an OP, etc.

The March draft versions of the ROPs suggest that the planned use of the TA priority is ambiguous and varies between programmes. Some ROPs limit the use of this priority solely to the activities defined under Article 44 of the General Regulation. To the contrary, the following regions mention pilot project funding and absorption capacity enhancement in their versions of ROPs:

- Central Bohemian region through the special Absorption Capacity priority, for which an indicative allocation is proposed amounting to 3% of the total eligible expenditure of the programme;
- Northwest region;
- Southeast region;
- Central Moravian region proposes the Absorption Capacity measure supporting development of integrated projects;
- Moravian-Silesian region.

For the OPs chosen as suitable for implementation of PPP projects, we recommend to extend the list of supported activities with model PPP projects and with support of absorption capacity in the form of PPP projects.

As for Prague, OP Competitiveness considers allocating 4% of the total eligible expenditure of the programme to the TA priority. The current financial plan suggests the allocation of CZK 406M, which represents a financial allocation similar to that of the ROPs. The above allocation should be spent on activities similar to those under ROPs.

## **7 Proposal of General Text on the Possibility to Apply the PPP Principle to Selected Operational Programmes**

“The public-private partnership (PPP) model has been newly supported by binding EC regulations stipulating conditions for drawing on the Funds in the programming period 2007-2013.

PPP projects are based on a long-term contractual relation in which the public and private sectors share benefits and risks arising from the provision of public infrastructure or services. The advantage of PPP is the combination of experience, knowledge and skills of both sectors and the transfer of risks to the sector that is able to manage them better.

In most cases the public sector delegates provision of a certain service to the private sector drawing on its organisational skills and expertise that are stimulated not only by the return on invested capital but also risk of its loss.

Generally, we may say that the objective of PPP projects is to develop a basic infrastructure that would serve the public interest and to provide suitable types of public services that the private sector is able to provide in a better quality (with regard to value for money), in a more efficient way and at a price acceptable for the public sector.

In justified cases it proves to be appropriate to implement PPP projects under operational programme measures. Prior to the approval of such projects the following conditions have to be met:

- The PPP project implementation will bring higher value for money for the public sector and higher quality of the project;
- The private sector will undertake risks that would have been borne by the public sector had the project not been implemented by PPP. The private sector is able to assess the risks under a stricter regime than the public sector.

The main reason for PPP projects is enhancing absorption capacity of the Czech Republic without putting similar burden on the budget as traditional public procurement. With the PPP model the settlement of the public sector liabilities resulting from the acquisition of investment is postponed to the phase when the investment is put into operation. The public entity contributes to financing the costs of the investment acquired and services provided (e.g. in the form of fees for availability) during the term of the concession agreement.

Characteristic elements of PPP projects co-financed under the Funds:

- Long-term duration of the project;
- public entity or SPV in the role of beneficiary;
- project financing from private as well as public sources, public sources meaning the Funds and national public funds;
- risks arisen from the investment implementation and operation shared by the public entity and the private sector partner, the public sector having guidance for risk management from the private sector;
- public services provided by the private investor in the phase of operation.

When selecting and implementing PPP projects it is necessary to pay special attention to the project preparatory phase consisting mainly of:

- Preparing engineering study;

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- carrying out project legal due-diligence;
- assessing benefits of the PPP alternative compared to traditional public procurement;
- calculating value for money;
- carrying out tender to select the private partner in compliance with the Public Procurement Act and the Concession Act;
- setting a clear guidance framework according to types of beneficiaries and projects considered that would be used for general PPP promotion and would show feasibility of meaningful co-operation of the public and private sectors and EU co-financing.

When preparing PPP projects, the provisions of the Public Procurement Act and the Concession Act must be observed, especially the rules of concession procedures, the eligibility of beneficiaries receiving contributions from the Funds and requirements for project eligible expenditure (i.e. to be financed under the Funds).

The PPP projects will be more demanding with regard to technical and administrative capacity during the implementation and management as well as monitoring and control activities. In case the beneficiary of the EU funding is a public entity, the concession agreement shall define data required from the private partner for monitoring and control activities.

The preparation of PPP projects under the OP priorities has to consider the system of annual allocations of funds under the OP and therefore set the project phases in compliance with these rules. On the other hand it is necessary to bear in mind that the total duration of the project can exceed 24 months and in extreme cases it can last for the whole programming period 2007-2013.

The public sector must be motivated to implement PPP projects. The PPP model shall be promoted more visibly and there will be active communication with the private sector.”

### **7.1 Specific Recommendations for the OP**

The above text, however, cannot be considered exhaustive with regard to the implementation of PPP projects financed under the Funds.

#### **7.1.1 Definition of Beneficiaries**

Generally for all operational programmes we recommend to extend the range of public entities eligible to act as beneficiaries. The public entity is entitled to a higher volume of grants under the Funds (max. 85% for a public entity whereas 40% for a private entity) and it can usually access a higher number of priorities across operational programmes compared to the number of priorities designed exclusively for private entities. The list of potential public entities:

- ministries, regions and municipalities (selected research and development departments can be beneficiaries);
- institutions receiving contributions from the State budget;
- institutions, within territorial self-governing units, which receive contributions from the State budget;
- organisational units of the State and of the territorial self-governing units;
- public research institutes, universities;
- legal entities owned by the State.

In addition, an SPV as a legal entity established exclusively to implement a specific PPP project should be included in all priorities in which PPP projects implementation is considered.

### 7.1.2 Eligibility of Expenditure

As it follows from other chapters of this study, PPP projects are more financially demanding in their preparatory phase requiring:

- preparation of a higher number of studies (e.g. engineering study, volume and architectural study, feasibility study – outline business case) being an integral part of the project documents;
- legal services connected with the organisation of a tender for a service supplier for PPP projects and with the conclusion of a concession agreement, which currently does not exist in a unified form and its essential elements have not been defined;

We recommend including the costs of this type directly in all priorities selected for the implementation of PPP projects.

The preparatory phase costs can be financed either under technical assistance in case the activities are included in OP Technical Assistance or activities supported under the priority Technical Assistance of the relevant operational programme. Another option is determining a percentage limit of total eligible expenditure to cover costs for project documents. In the current programming period this limit was 5% of total eligible expenditure while for the purposes of the PPP project it is necessary to increase it to at least 15% of total eligible expenditure.

### 7.1.3 Time Schedule for the Project Implementation

The operational programmes usually define maximum project duration. With regard to time requirements for the preparatory and implementation phases we recommend to define duration of the selected priorities for PPP projects to be the whole programming period, i.e. from the submission of the operational programme in the course of 2006 to the date of final payment (approximately July 2015).

### 7.1.4 Essential Elements of Project Documents

We assume that the project documents will include:

- feasibility study;
- outline business case (including cost-benefit analysis);
- budget of the project;
- effective zoning decision;
- environmental impact assessment;
- draft concession agreement including provisions relevant for the drawing on the Funds;
- beneficiary ownership structure.

PPP projects are characterised by setting binding conditions for the project investment and operational phase when tender is prepared for the project. Therefore, the project application evaluator should have at his/her disposal **draft or final concession agreement** clearly stipulating the following:

- title of ownership to the investment;
- type of financing structure – use of interim payments or payments after the investment is put into operation;

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- provision of accounting documents, records and information in the scope necessary for the preparation of monitoring reports;
- enabling access to the investment, enabling access to the seat of the private entity and submission of accounting documents, records and information in order for the authorised entities to perform on-the-spot checks;
- stipulation of reasons for withdrawal from the concession agreement and the consequences thereof;
- delimitation of impacts on financing in case of major changes in the project functioning as a safeguard for potential claims for the return of grants – there is a real risk that an amendment to the agreement is adopted in the course of drawing grant under the Funds that would essentially change the conditions for the PPP project implementation. In such a case the managing authority shall be informed in advance and the beneficiary must wait for its opinion.
- risk sharing between the public and private entities.

The managing authority shall always assess separately whether the beneficiary must be included under the concept of an undertaking with regard to state aid and identify relevant restrictions.

## **8 Implementation of the Model PPP Project Co-financed under the Funds - “Jihlava Polytechnic CAMPUS”**



## **8.1 Introduction**

### **8.1.1 Project Title**

**Jihlava Polytechnic CAMPUS**

### **8.1.2 Purpose of the Model Project**

The purpose of the model project (hereinafter “the Model Project”) is to assess positive and negative impacts of the submitted project implementation by meaningful combination of funds from the university budget, the EU Structural Funds and the private sector. The result is to assess the Model Project effectiveness based on the above combination of funds.

The Model Project was prepared as part of the study on the Application of the PPP Principle on the Economic and Social Cohesion Policy conducted by the consortium of Deloitte CZ, Elbona, the Havel & Holásek law firm and CopiRisco CZ based on the results of a tender called for by the Ministry for Regional Development.

### **8.1.3 Model Project Rationale**

The Jihlava Polytechnic CAMPUS model project was selected by the project author as a relevant example of a project actually prepared in the Czech Republic and it was approved by the contracting authority. The original idea to use some of the reference projects implemented in the selected EU countries proved to be wrong in the course of the preparation of the “Application of the PPP Principle on the Economic and Social Cohesion Policy” project. The originally presented “Vasco de Gama Ponte” project was described by the Ministry of Transport and will be further analysed for the purposes of the Ministry of Transport. The second originally presented “Amador-Sintra Hospital” project is not suitable since the system of drawing on the Funds in Portugal significantly differs from the Czech system and the described project would not fulfil the requirement of the Ministry for Regional Development, i.e. demonstrating the combination of PPP and the EU funding. Based on an agreement with the Community Support Framework Department it was decided to select a project under preparation in the Czech Republic and describe the possibility of combining the EU and PPP funding. Upon detailed evaluation of several projects the author selected the Jihlava CAMPUS since this project had already been under preparation and it was possible to get a very specific idea about its output. Furthermore, it pertains to the area of social infrastructure, human resource development and scientific research and development which is an area that will certainly develop in the Czech Republic. The Jihlava CAMPUS project can be included in the category of small- to medium-sized projects and it can become a good model for other draft projects being prepared to be implemented in the programming period 2007-2013 in the sectors of education or public administration reform. The above projects, Vasco de Gama Ponte or Amadora-Sintra, are major projects of a type that would be addressed under the Cohesion Fund in the Czech Republic as transport or environmental projects. Therefore, the CAMPUS Jihlava project is a logical complement to the already described projects striving for different combinations of PPP and EU funding.

### 8.1.4 Identification of the Model Project Vehicle

Table 1: Identification of the Model Project Vehicle

Identification of the Feasibility Study Supplier	
<b>Name</b>	Jihlava Polytechnic
<b>Business ID/Tax ID</b>	71 22 64 01 / CZ 71 22 64 01
<b>Legal status</b>	University
<b>Registered seat</b>	Tolstého 16, Jihlava, 586 01, Czech Republic
<b>Contact address</b>	Tolstého 16, Jihlava, 586 01, Czech Republic
<b>Official website</b>	<a href="http://www.vspji.cz">www.vspji.cz</a>
<b>Project contact person</b>	Ladislav Jirků – President of the Jihlava Polytechnic
<b>Tel.:</b>	+420 567 141 111
<b>Fax:</b>	+420 567 310 181
<b>E-mail:</b>	<a href="mailto:jirku@vspji.cz">jirku@vspji.cz</a>

## 8.2 Brief Overview of Objectives

### 8.2.1 Project Background

One of the main objectives of the Jihlava Polytechnic is to build a university CAMPUS on the premises at Legionářů 9, Jihlava (former hospital) that was transferred to the University free of charge by the Vysočina region as a development potential supporting university education in the Vysočina region. The urban concept of the CAMPUS development also counts on the premises at Tolstého 16 (current University seat), adjacent to the Legionářů premises.

The development of the CAMPUS will help to create attractive environment for Czech as well as foreign students as well as for students coming from commercial institutions and companies of the industries that would benefit from co-operation with the University, thus providing for a synthesis between the academic, practical and business spheres, or other activities the new premises would be suitable for. The CAMPUS will not only be a place of studies and research and development activities, it will also provide accommodation, board, entertainment, leisure activities, shopping opportunities and various sports and social activities for students and faculty members, congress participants, etc. The development includes the following investment and non-investment projects:

- Teaching premises (5 seminar rooms – 125 seats, 2 lecture halls – 400 seats), regional scientific library and study halls (50,000 pcs of library items, 200 seats for students)
- Multipurpose hall (300 seats), gymnasium, space for leisure time, technical rooms for education, research and development (10 work rooms, laboratories)
- Canteen (1,000 meals, 250 seats) – located in the current main building after its conversion
- Residence halls (700 beds) including other facilities (study rooms, fitness centre, etc.)

### 8.3 Identification of Beneficiaries

Contrary to financial flow analysis the economic analysis includes socio-economic drawbacks and benefits whose beneficiary is not only the project vehicle but society in general, since it will be impacted by the project, which is relevant from the point of view of the intended objective.

Following is a list of beneficiaries relevant from the viewpoint of interest of the beneficiary, grant provider and the private sector as the project co-investor. The impact on these beneficiary groups will be assessed in the Model Project description below. The project evaluation will assess especially the impact on the local level, impact on the project finance and sustainability.

Beneficiaries:

- Jihlava Polytechnic students
- Jihlava Polytechnic faculty (including university staff)
- Private investor of the development
- Operator (can be identical to the investor)
- Employers in the region

Further on, we shall define social and economic costs and benefits for individual beneficiaries in case the JIHLAVA CAMPUS is developed and put into operation.

Table 2: Project Impacts

Project impacts	
University students	Better quality facilities for studies (new teaching premises, multipurpose hall and library), possibility to test theoretical knowledge in practice (laboratories and technical rooms), high quality accommodation and board at reasonable price (residential halls for 700 students and a canteen)
Faculty	Better quality facilities for teaching (new teaching premises, multipurpose hall and library), possibility to use new equipment and technologies for teaching (laboratories and technical rooms), high quality accommodation and board during stay at the university (canteen and residential halls)
Private investor	Based on tender results, implementation of the construction part of the project, generation of profit.
Operator	Operation of the CAMPUS and generation of long-term profit from fees paid for using the project.
Employers in the region	With regard to close links to strong employers in the region (Bosch, Tesla Jihlava, Jihlavan, and others) the development of the CAMPUS will enhance the University position in the region as a source of high quality workforce with theoretical as well as practical skills.

Source: Deloitte, CopiRisco CZ, Havel & Holásek, Elbona Consortium

### 8.3.1 Real Financial Limits

Total project costs are budgeted as follows:

• Construction costs – residential halls	CZK 250,000,000
• Construction costs – multipurpose hall	CZK 15,000,000
• Construction costs – canteen	CZK 85,000,000
• Construction costs – laboratories	CZK 42,000,000
• Construction costs – library	CZK 65,000,000
• Equipment costs – residential halls	CZK 100,000,000
• Equipment costs – multipurpose hall	CZK 5,000,000
• Equipment costs – canteen	CZK 35,000,000
• Equipment costs – laboratories	CZK 55,000,000
• Equipment costs – library	CZK 20,000,000
• Other costs – residential halls	CZK 10,000,000
• Other costs – multipurpose hall	CZK 1,000,000
• Other costs – canteen	CZK 2,000,000
• Other costs – laboratories	CZK 12,000,000
• Other costs – library	CZK 3,000,000
Total acquisition costs	CZK 700,000,000
• Operating costs (annual) – residential halls	CZK 9,000,000
• Operating costs (annual) – multipurpose hall	CZK 1,000,000
• Operating costs (annual) – laboratories	CZK 3,500,000
• Operating costs (annual) – library	CZK 1,000,000
Total annual operating costs	CZK 14,500,000

## 8.4 Financial Flows Analysis

The analysis was made based on the inputs indicatively determined by the author. With regard to the purpose of the Model Project preparation the absolute values of individual indicators are not as important as their inclusion in analysis and their development.

### 8.4.1 Project Cash Flow Overview under the Financial Analysis

Table 3: Project Impacts

Period	2007
1 Land	0
2 Buildings and structures	
Residential halls	250,000
Multipurpose hall	15,000
Canteen	85,000
Laboratories	42,000
Library	65,000
3 New interior equipment (depreciated)	
Residential halls	100,000
Multipurpose hall	5,000
Canteen	35,000
Laboratories	55,000
Library	20,000
4 Used equipment	0
5 Extraordinary maintenance	
<b>6 Fixed assets</b>	<b>672,000</b>
7 Administrative costs (EU funds)	1,000
8 Costs of tender	2,000
9 Costs of the preparation of application	2,000
10 Other costs	
Residential halls	10,000
Multipurpose hall	1,000
Canteen	2,000
Laboratories	12,000
Library	3,000
<b>11 Investment costs ( A )</b>	<b>700,000</b>
12 Cash money	0
13 Low-value fixed assets	0
14 Current liabilities	
15 Net working capital	
<b>16 Working capital variance ( B )</b>	<b>0</b>
17 Depreciation and changes	
18 Residual value	
<b>19 Other investment items ( C )</b>	<b>0</b>
<b>Total investment costs (A+B+C)</b>	<b>700,000</b>

## 8.5 EU Financing

When looking for appropriate Funds for the implementation of the JIHLAVA CAMPUS project we draw on the status of operational programmes as at March 2006, i.e. in the phase of first draft versions of operational programmes when proposals of priorities were presented but detailed specifications of supported activities, distribution of financial allocations among the relevant priorities, identification of beneficiaries, definition of financial limits per project size and list of eligible expenditure were lacking. Since the individual operational programmes are still in the process of preparation the above information must be taken as such.

Two operational programmes have been selected as appropriate for financing the JIHLAVA CAMPUS investment proposal, namely:

- OP Research and Development for Innovation (hereinafter the “R&DI”), Priority 1: Fostering R&D capacities and their integration to the European Research Area (ERA), Measure 1.1: Fostering R&D capacities;
- Regional Operational Programme (ROP) of the Southeast region, Priority 4: Human resource development, Measure 4.3: Infrastructure for human research development.

The R&DI programme will be used for financing the acquisition of R&D infrastructure, including laboratories and technical equipment. The laboratories will be used for research and development in machine engineering and IT, i.e. in certified study fields of the Jihlava Polytechnic. Since the University closely co-operates with local businesses the R&D results will focus mainly on the micro-machine engineering (as an example we can mention several-year close co-operation with BOSCH Jihlava, TESLA Jihlava, Jihlavan, etc.). The co-operation between the public and private sectors started with the foundation of the University and it mainly offers semi-annual fellowship programmes. However, it encounters a problem with insufficient background facilities lacking state-of-the-art technical equipment for research development and its application. Therefore, we consider R&DI a good opportunity for progressive development in the innovation area and for enhancing economic level and business competitiveness compared to other regions and for the creation of jobs.

A suitable beneficiary of grants under the Funds could be the public university or private R&D institutes meeting criteria pursuant to S. 28(3) of Act No. 130/2002 Coll. The project is also interesting for the beneficiaries with regard to its ceiling for allocation of contribution (EU or national financing). The projects in the field of R&D are permitted the public financing in the full amount, i.e. 100%, provided the income generated from innovation activities is reallocated to research.

The project achieves the required financial ceiling for eligible expenditure that has been stipulated between CZK 100M and 1.5bn under Measure 1.1.

The Regional Operational Programme (ROP) of the Southeast region, Priority 4: Human resource development, Measure 4.3: Infrastructure for human resource development is an appropriate programme for the Jihlava Polytechnic University. Under this programme it is possible to apply for a grant for the Campus library, multipurpose hall, gymnasium, canteen and residential halls. The minimum limit for eligible expenditure under this programme has not been defined yet, unlike in the R&DI programme, and the author of the operational programme believes such limit will not be defined. Pursuant to the proposal of March 2006 the rate of EU and public financing has been set to 85% and 15% co-financing of the beneficiary.

## 8.6 Calculation of the EU Contribution to the Jihlava CAMPUS Project

### 8.6.1 Financing under OP Research and Development for Innovation

The Jihlava CAMPUS project is composed of several parts potentially to be financed under different EU operational programmes. OP Research and Development for Innovation can be used for financing future CAMPUS laboratories and their equipment. (This study is based on the OP R&DI version as at 22 February, 2006). Since the beneficiary is a public entity, whose purpose under the Act on Universities also includes research activities, it can be awarded a grant in the amount up to 100% of eligible expenditure provided that all potential income from research and development is reinvested in the laboratories and study halls in the form of purchase of new equipment or technologies. Under this condition the project can be considered as not generating revenues.

Eligible Expenditure under the R&DI Operational Programme Pursuant to Government Resolution No. 461/2002 Coll.

- personnel costs or expenditure connected with R&D staff, university staff, technicians and other support staff. The personnel costs or expenditure may include
  - wages or salaries of staff recruited with an employment contract exclusively for the project
  - relevant part of wages or salaries of staff with regard to their time allocation for the work on the project or co-operation on the project
  - increase of a flexible part of wage or salary of staff collaborating on the project
  - other personnel costs or expenditure based on an Agreement to Perform Work or Agreement to Complete a Job concluded directly for the project
- costs or expenditure of beneficiary or co-beneficiaries for acquisition of tangible assets used directly for the project whose amount is defined as follows
  - amount of eligible expenditure for the acquisition of fixed tangible assets with a period of life cycle longer than the project term or for acquisition of tangible assets whose acquisition price is higher than CZK 40,000 and life cycle longer than one year and at the same time longer than the project term is calculated using the following formula:

$$EC = (A/B) * C * D$$

where:

EC is eligible costs

A is time in years for which the assets will be used for the purposes of the project

B is time of the asset life cycle in years defined pursuant to special legal instruments

C is asset acquisition price defined pursuant to a special legal instrument

D is share of the assets used for the project

In the case of the Jihlava CAMPUS we come to the following result:

$$\text{Eligible costs of equipment} = (5/5) * \text{CZK } 54,000,000 * 1 = \text{CZK } 54,000,000$$

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Eligible costs of construction = (30/30) \* CZK 55,000,000 \* 1 = CZK 55,000,000

**Rationale**

The Jihlava Polytechnic focuses on R&D in micro-machine engineering and if its results are to be used in practice, the University necessitates state-of-the-art technology equipment, i.e. it must dispose of obsolete laboratory equipment, therefore we assume that the assets will not be used longer than five years. Item B is based on the equipment accounting depreciation group, which equals five years.

**8.6.2 Financing under the Regional Operational Programme, Measure 4.3. Infrastructure for Human Resource Development**

Another part of the Jihlava CAMPUS project is the construction of a multipurpose hall, canteen, gymnasium and residential halls. This part of the CAMPUS, contrary to the laboratories, shall generate the following expected revenue (indicatively determined):

	<b>Building</b>	<b>Investment</b>	<b>Annual Revenue</b>
1	Library	88,000,000	450,000
2	Hall	7,000,000	100,000
3	Study Hall	7,000,000	50,000
4	Gymnasium	7,000,000	150,000
5	Canteen	122,000,000	10,000,000
6	Residential Halls	360,000,000	13,000,000

The current value of total investment costs is CZK 591,000,000 and discounted value (by 6%) of net revenue including the residual value is CZK 382,000,000

**Determining the Jihlava CAMPUS Project Co-financing Rate under the ROP**

The new Regulations stipulating ceiling of co-financing rates explicitly require setting of these ceilings thus reflecting whether the project is or is not a revenue-generating project. The basis for this is determining the “financial gap or financial deficit” and overcoming this gap using the EU grants.

Calculation:

$$R = (DIC - DNR) / DIC$$

$$DA = EC * R$$

$$EU \text{ grant} = EC * DA$$

where:

R is financial gap rate

DA is co-financing rate

DIC is discounted investment costs

DNR is discounted net revenue, calculated as discounted revenue minus discounted operating costs + discounted residual value

EC eligible costs

EU grant is the amount of grant under the Funds

The case of the Jihlava CAMPUS:

$$R = (591\,000\,000 - 382\,000\,000) / 591\,000\,000 = 35,5 \%$$

$$DA = 35,5\% * 591\,000\,000 = 209\,805\,000$$

$$EU \text{ grant} = 209\,805\,000 * 85 \% = 178\,334\,000 \text{ CZK}$$

### 8.6.3 Overview of the EU Financing of the Jihlava CAMPUS

The following values were reached as a result of total evaluation of potential financing options:

#### Laboratories – construction part:

Expected investment:	CZK 55,000,000
Grant:	CZK 55,000,000 (100%)
Other operating costs:	CZK 3,500,000

#### Laboratories – equipment:

Expected investment:	CZK 54,000,000
Grant:	CZK 54,000,000 (100%)

#### Multipurpose hall, gymnasium, study halls, residential halls:

Expected investment:	CZK 591,000,000
Grant:	CZK 178,334,000
Other operating costs:	CZK 11,000,000

<b>Total funding:</b>	CZK 287,334,000 under the Funds
	CZK 412,666,000 from other resources (Jihlava Polytechnic University, Ministry of Education, Youth and Sports, private resources)

## 9 Recommendations

Draft Recommendations for the application of PPP projects financed under the Funds in the programming period 2007-2013.

Barrier	Recommendations
<b>Restrictions related to beneficiaries and the ownership structure</b>	<p><b>Main recommendations on the programming level with a link to the Commission</b></p> <ul style="list-style-type: none"> <li>• Ownership of infrastructure by the private beneficiary in the course of the operational phase provided the project objective is not changed for the time of its sustainability. If the Commission rejects the possibility to transfer the title of ownership from the public to the private entity during the sustainability phase, we recommend organising separate tenders for supplier in the investment and operational phases.</li> </ul>
<b>Project cash flow</b>	<p>In order to provide for effective combination of PPP and the Funds in the programming period we recommend to start technical consultations with the Commission in order to clarify the interpretation of the following:</p> <ul style="list-style-type: none"> <li>• eligible expenditure will be paid by the beneficiary within the programming period;</li> <li>• payment of project investment costs in the operational phase (i.e. “the infrastructure component”).</li> </ul>
<b>Revenue-generating projects</b>	<ul style="list-style-type: none"> <li>• Revenue-generating projects should not include projects generating revenues from shadow toll and fees for infrastructure/service availability paid by the public entity to the private entity;</li> <li>• Negotiations with the Commission regarding inclusion of PPP projects in the group of revenue-generating projects and the precise construction of Article 54(4) of the General Regulation, with regard to who would be responsible for returning of the respective amount to the EU budget and how to proceed in such a case. Technical workshops with DG Regio and meetings of representatives of the Visegrad Countries should be used for communication with the Commission.</li> </ul>
<b>Generation of improper profit</b>	<ul style="list-style-type: none"> <li>• Incorporation of binding conditions arising from the above Information notes in the concession agreement in the case of a specific project.</li> <li>• Identification of specific criteria based on which exceeding the recommended value of internal rate of return in individual sectoral areas could be justified.</li> <li>• Preparation of a detailed Outline Business Case at the beginning of the project including estimate of acceptable profitability enabling co-financing under the Funds as recommended in the Guide to Cost-Benefit Analysis of Investment Projects and in Information notes 58 and 64.</li> </ul>

<b>Main recommendations on the programming level with a link to the Government, ministries and managing authorities</b>	
<b>Barrier</b>	<b>Recommendation</b>
<b>Procedures contrary to law in public procurement</b>	<ul style="list-style-type: none"> <li>• Training of the responsible staff.</li> <li>• Setting up control mechanisms and standard procedures in order to make the process transparent.</li> <li>• In the case of major projects (most PPPs) use private consultants               <ul style="list-style-type: none"> <li>▪ responsibility for correct procedure, if not complied with, financial recourse can be applied easily</li> <li>▪ consultant guarantees the quality.</li> </ul> </li> </ul>
<b>Contradiction between compatibility of PPP and state aid rules</b>	<ul style="list-style-type: none"> <li>• In the project preparatory phase apply such procedures that would identify potential state aid on a regular basis:               <ul style="list-style-type: none"> <li>▪ state aid will be consequently eliminated</li> </ul> </li> <li>• state aid will be accepted within the Czech Republic and the relevant steps in compliance with the Community law will be taken.</li> </ul>
<b>Project cash flow</b>	<ul style="list-style-type: none"> <li>• Start project preparation sufficiently in advance.</li> <li>• Perform detailed feasibility study of the project before processing an application for grant approval.</li> <li>• Prevent the risk of deviation from the expected timing and grant amount in the contractual documents (conditions precedent, risk assessment and allocation).</li> <li>• When using interim payments provide for sufficient motivation of the private entity to complete the project.</li> <li>• Possibility for the beneficiary to use interim payments, but the beneficiary shall be sent the grant payment on the blocked account that would be released only after the infrastructure/service has been handed over for use. The beneficiary shall deposit the grants allocated under the Funds on the blocked account of a private entity (provider) with the right to draw the money only when contractual conditions under the concession agreement have been duly met.</li> <li>• Clarification of the system for reporting project and programme financial indicators (ISPROFIN is based on reporting technical parameters while PPP projects are based on the principle of providing service) and of accounting issues pertaining to PPP projects</li> </ul>

<b>Main recommendations on the programming level with a link to the Government, ministries and managing authorities</b>	
<b>Barrier</b>	<b>Recommendation</b>
<b>Absorption capacity of PPP projects</b>	<ul style="list-style-type: none"> <li>• Major infrastructure projects, mainly in the fields of transport and the environment are most suitable for effective combination of PPP and EU financing (investment costs &gt; CZK 1bn)</li> <li>• Unified definition of PPP projects on the ministerial level and unified approach to the preparation and implementation of PPP projects;</li> <li>• Realistic assessment of opportunities under individual operational programmes and consequent selection of PPP projects suitable for co-financing under a specific operational programme;</li> <li>• Performing detailed selection of PPP projects as soon as possible;</li> <li>• Preparing an indicative list of potential PPP projects combined with the Funds in the Czech Republic (per individual operational programmes) on the level of managing authorities;</li> <li>• Preparing standard documents with regard to PPP projects (tender dossier, concession agreements – standard provisions pertaining to the Funds);</li> <li>• Mapping private sector interest (including identification of priority areas)</li> </ul>

<b>Main recommendations on the programming level with a link to managing authorities</b>	
<b>Barrier</b>	<b>Recommendation</b>
<b>Fiche deviation risks</b>	<ul style="list-style-type: none"> <li>• Incorporate the deviation already into the NSRF or an operational programme to be approved by the Commission <ul style="list-style-type: none"> <li>▪ risk – the Commission will not approve it and the OP will have to be changed.</li> </ul> </li> </ul>
<b>Restrictions related to beneficiaries and the ownership structure</b>	<ul style="list-style-type: none"> <li>• Propose the ownership structure always for a specific project.</li> <li>• Consider financing restrictions always with regard to different categories of beneficiaries and different PPP structures.</li> </ul>
<b>Restrictions on expenditure eligible for financing under SF</b>	<ul style="list-style-type: none"> <li>• Use the Funds to cover costs in the project preparatory and investment phase.</li> <li>• Draw funds for the project preparatory phase from technical assistance, the Jaspers initiative (use Jaspers especially for financial analysis consultations in case of major projects) and we also recommend to increase the percentage limit for costs of project documents within eligible expenditure.</li> <li>• Incorporation of specific PPP project costs (e.g. engineering study, volume and architectural study, legal services during organisation of a tender for a private entity or set up of an SPV) into the “Eligible Expenditure” manual. We assume that even though the Funds are considered national funding there will be a unified methodology defining eligible expenditure for individual funds (ERDF, ESF, CF).</li> </ul>

<b>Main recommendations on the programming level with a link to managing authorities</b>	
<b>Barrier</b>	<b>Recommendation</b>
<b>Beneficiary</b>	<ul style="list-style-type: none"> <li>We prefer a public entity to be a potential beneficiary for a grant under the Funds since it is entitled to a higher amount of grant under the Funds and is subject to control in compliance with Act 320/2001 Coll., on financial audit in public administration.</li> <li>As for private entity the amount of state aid must not exceed the 40% limit in compliance with the Regional Map of State Aid Intensity, with the exception of approved block exceptions.</li> </ul> <p>Definition of suitable groups of potential beneficiaries that would be in the role of PPP contracting authorities and would have access to drawing grants under the Funds. We recommend that the group of potential beneficiaries includes the following:</p> <ul style="list-style-type: none"> <li>ministries, regions and municipalities (selected research and development departments can be beneficiaries);</li> <li>institutions receiving contributions from the State budget;</li> <li>institutions, within territorial self-governing units, which receive contributions from the State budget;</li> <li>organisational units of the State;</li> <li>public research institutes, universities;</li> <li>legal entities owned by the State.</li> </ul> <ul style="list-style-type: none"> <li>Generally we can recommend that the group of potential beneficiaries is as widely defined as possible.</li> </ul>
<b>Risk of misuse of the Funds and return of the grant</b>	<ul style="list-style-type: none"> <li>The risk of misuse of the Funds is linked to the need for each specific project to present clear justification (rationale) for using the grants under the Funds (the costs must be indicated in the feasibility study or a detailed budget of the project).</li> </ul>
<b>Control mechanisms and monitoring</b>	<ul style="list-style-type: none"> <li>Incorporation of information requirements on the part of the private investor to the concession agreement.</li> <li>Identification of specific indicators (such as e.g. monitoring indicators) based on the decision to award a grant and definition of conditions for control and monitoring in the course of the project implementation directly under the concession agreement.</li> <li>When defining information requirements and control mechanisms, proceed in compliance with the Personal Data Protection Act.</li> </ul>
<b>Wrong project implementation timing</b>	<ul style="list-style-type: none"> <li>Define project phases together with time delays compared to the timing in the evaluation phase and project administration and subsequent payment of grants under the Funds (especially preparatory and investment phases).</li> <li>Set up realistic timing for PPP project implementation and provide for the beginning of the project immediately after the call for proposals and provide for on-going calls.</li> <li>Begin with tender for concessionaire before the registration of applications for contribution under the Funds, i.e. know the final supplier of works/services prior to signing the financing contract.</li> <li>In relation to the new system of financial flows via the state budget adjust the timing for approval of payment claims and for payment of grants to the beneficiary’s account.</li> </ul>

Main recommendations on the programming level with a link to managing authorities	
Barrier	Recommendation
Implementation structure	<ul style="list-style-type: none"> <li>• Expand the implementation structure roles and responsibilities pertaining to PPP projects:                             <ul style="list-style-type: none"> <li>▪ define the roles of entities incorporated in the implementation structure for the CF with link to PPP projects.</li> </ul> </li> <li>• Enhance institutional and administrative capacity and expertise on the part of the public sector.</li> </ul>

Main recommendation on the project level with a link to managing authorities	
Barrier	Recommendation
Operational programmes and manuals for beneficiaries	<p>We recommend to describe characteristic elements of PPP projects co-financed under the Funds in the operational programmes:</p> <ul style="list-style-type: none"> <li>• long-term duration of the project</li> <li>• public entity or SPV in the role of beneficiary (or another entity not complying with the definition of an "undertaking" according to the state aid rules)</li> <li>• project financing from private as well as public sources, public sources meaning the Funds and national public financing</li> <li>• risks arisen from the investment implementation and operation shared by the public entity and the private sector partner, the public sector having guidance for risk management from the private sector</li> <li>• public services provided by the private investor in the phase of operation.</li> </ul>
	<p>We recommend to incorporate the following essential elements in the operational programme and manuals for beneficiaries:</p> <ul style="list-style-type: none"> <li>• Identification of beneficiary (see bullet point Beneficiary)</li> <li>• Definition of eligible expenditure (see bullet point Restrictions on expenditure eligible for financing under SF)</li> <li>• Essential elements of project documents                             <ul style="list-style-type: none"> <li>○ Feasibility study;</li> <li>○ outline business case (including cost-benefit analysis);</li> <li>○ budget of the project;</li> <li>○ effective zoning decision;</li> <li>○ environmental impact assessment;</li> <li>○ draft concession agreement including provisions relevant for the drawing on the Funds;</li> <li>○ beneficiary ownership structure.</li> </ul> </li> </ul>

## 10 Annex No. 1: List of Basic Types of PPP Structures

<b>List of Basic Types of PPP Structures</b>	
1.	<p><b>Build-Own-Operate (BOO)</b></p> <ul style="list-style-type: none"> <li>• SPV (“Special Purpose Vehicle”: a private entity founded for the purposes of implementing a PPP project) finances and builds an infrastructure project.</li> <li>• When the construction is completed the SPV owns and operates the infrastructure for the whole period of its life cycle.</li> <li>• SPV generates revenues from the project operation.</li> </ul>
2.	<p><b>Build-Operate-Transfer (BOT)</b></p> <ul style="list-style-type: none"> <li>• SPV finances and builds the infrastructure.</li> <li>• SPV builds the infrastructure, operates it for a limited time period (usually 20-40 years) and generates revenues from the project operation.</li> <li>• At the end of this period the right of ownership is transferred to the public sector.</li> </ul>
3.	<p><b>Design-Build-Finance-Operate (DBFO)</b></p> <ul style="list-style-type: none"> <li>• SPV finances and builds the infrastructure.</li> <li>• SPV owns the infrastructure during the construction period but upon its completion it transfers it to the public sector.</li> <li>• The infrastructure is operated by the SPV for a limited time period (usually 20-40 years).</li> </ul>
4.	<p><b>Build-Lease-Operate-Transfer (BLOT)</b></p> <ul style="list-style-type: none"> <li>• SPV builds the infrastructure on the land owned by the public sector financing its construction.</li> <li>• Upon the completion of construction the SPV operates the infrastructure and receives fixed lease instalments from the public sector.</li> </ul> <p>At the end of the leasing period (usually 20-40 years) the infrastructure is transferred to the public sector.</p>
5.	<p><b>Design-Build-Maintain (DBM)</b></p> <ul style="list-style-type: none"> <li>• SPV designs and builds the infrastructure.</li> <li>• The public sector owns the infrastructure for the whole period.</li> <li>• SPV maintains the infrastructure and receives fees for availability from the public sector.</li> </ul>
6.	<p><b>Design-Build-Operate (DBO)</b></p> <ul style="list-style-type: none"> <li>• SPV designs and builds the infrastructure.</li> <li>• The public sector owns the infrastructure for the whole period.</li> <li>• SPV operates the infrastructure and receives fees for availability from the public sector.</li> </ul>

## 11 Annex No. 2: List of Meetings Held

Government Authority	Date	Person
Ministry of the Environment	2/2/2006	Ing. Petr Novák
Prague City Council	2/2/2006	Mgr. Patricia Ferulíková
Ministry of Culture	3/2/2006	Ing. Aleš Grof
Ministry of Foreign Affairs	3/2/2006	Ing. Jan Jursa
Ministry of Labour and Social Affairs	3/2/2006	Ing. Ivana Projsová
Ministry of Informatics	3/2/2006	Ing. Martin Hiršal
Ministry of Industry and Trade	6/2/2006	Ing. Tomáš Říčka, Ing. Petr Jaroš, Ing. Petr Ondráček, Ing. Petr Serafín
Central Bohemia Regional Authority	9/2/2006	Mgr. Marek Kupsa
Ministry of Education, Youth and Sports	9/2/2006	PhDr. Kateřina Pösingerová, CSc.
Ministry of Transport	10/2/2006 8/3/2006	Ing. Olga Pokorná
Ministry of the Environment	10/3/2006	Ing. Zdeněk Zelený
Government Office, R&D Section	13/3/2006	Dr. Marek Blažka
Ministry of Finance	15/3/2006 20/3/2006	Ing. Hloušek Ing. Kateřina Helikarová

## 12 Annex No. 3: List of Used Acronyms and Terms

List of Used Acronyms and Terms	
BLOT	Type of PPP model – Build-Lease-Operate-Transfer
BOO	Type of PPP model – Build-Own-Operate
BOT	Type of PPP model – Build-Operate-Transfer
CF	Cohesion Fund
CSG	Community Strategic Guidelines
DBFM	Type of PPP model – Design-Build-Finance-Maintain
DBFO	Type of PPP model – Design-Build-Transfer-Operate
DBM	Type of PPP model – Design-Build-Maintain
DBMO	Type of PPP model – Design-Build-Maintain-Operate
DBO	Type of PPP model – Design-Build-Operate
ECJ	European Court of Justice
EIB	European Investment Bank
EIF	European Investment Fund
ERDF	European Regional Development Fund
ESC policy	Economic and social cohesion policy
ESF	European Social Fund
Fiche No. 18	Information sheet n. 18 rev1 : Revenue-generating projects
Fiche No. 53	Fiche 53: Public-private participation: 2007-2013
Fiche No. 64	Guidance on the methodology for carrying out the cost-benefit analysis
ICT	Information and communication technologies
IOP	Integrated operational programme
IRR	Internal rate of return
JROP	Joint Regional Operational Programme
Low-value TFA	Low-value tangible fixed assets
MoF	Ministry of Finance
MoT	Ministry of Transport
NGO	Non-governmental organisation
NSRF	National Strategic Reference Framework
OBC	Outline business case
OP	Operational programme
PFI	Private Finance Initiative (a private sector partner operates and maintains infrastructure for a public body, the fees are not paid by the users but by the public entity)
PPA	Public Procurement Act
PPP	Public-Private Partnership
PSC	Public sector comparator
ROP	Regional Operational Programme
SME	Small- and medium-sized enterprise
SPD	Single Programming Document
SPV	Special purpose vehicle (a special legal entity created only for the purposes of fulfilling the tasks of a concessionaire)
TEN-T	Trans-European Transport Networks
TFA	Tangible fixed assets
the Commission	European Commission
the Funds	European Regional Development Fund, European Social Fund and Cohesion Fund
ÚOHS	Office for the Protection of Competition
WWTP	Waste water treatment plant

## 13 Annex No. 4: References

### **EC documents for the preparation of drawing on the EU funds in the 2007-2013 programming period:**

Cohesion Policy in Support of Growth and Jobs: Community Strategic Guidelines, 2007-2013

DIRECTIVE 2004/17/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL coordinating the procurement procedures of entities operating in the water, energy, transport and postal services sectors

DIRECTIVE 2004/18/EC OF THE EUROPEAN PARLIAMENT AND OF THE COUNCIL on the coordination of procedures for the award of public works contracts, public supply contracts and public service contracts

Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions (European Commission)

Proposal for a Council Regulation laying down general provisions on the European Regional Development Fund, the European Social Fund and the Cohesion Fund – Presidency compromise

Proposal for a Regulation of the European Parliament and of the Council on the European Social Fund – Presidency compromise

Proposal for a Regulation of the European Parliament and of the Council on the European Regional Development Fund (ERDF)

Proposal for a Regulation of the European Parliament and of the Council establishing a European grouping of territorial co-operation (EGTC)

Draft National Development Plan of the Czech Republic 2007-2013 (Ministry for Regional Development)

REVENUE-GENERATING PROJECTS Information sheet n. 18 rev1 (Fiche No. 18)

Public-private participation: 2007-2013 (Fiche No. 53)

Fiche No. 64 Guidance on the methodology for carrying out the cost-benefit analysis

Fiche No. 58 Clarification about the main questions raised

Fiche No. 60 Improved access to finance for micro business and SMEs in the regions of the EU

Fiche No. 61 JESSICA: Sustainable development for urban areas

Commission interpretative communication on concessions under Community law

### **Documents for the current programming period:**

Preparation of the Regional Operational Programmes in the Czech Republic (Source document of regions associated in NUTS II statistical units for negotiations on allocations for operational programmes 2007-2013)

Operational Programme Transport (Ministry of Transport)

**Final Report on Project 1p/05 – “Application of the PPP Principle on the Economic and Social Cohesion Policy” dated 15 May, 2006**

Operational Programme Environment 2007-2013 (Ministry of the Environment)

Operational Programme Infrastructure (Ministry of Transport, Ministry of the Environment)

Operational Programme Prague – Adaptability (Prague City Council)

Operational Programme Prague – Competitiveness (Prague City Council)

Operational Programme Business and Innovation 2007-2013 (Ministry of Industry and Trade of the Czech Republic)

Operational Programme Human Resources and Employment (Ministry of Labour and Social Affairs)

Operational Programme Research and Development for Innovation (Innovation and Knowledge Economy WG)

Operational Programme Research and Development for Innovation (source document for negotiations with the Commission bodies)

Operational Programme Research and Development for Innovation (Convergence objective, European Regional Development Fund, Managing Authority – Ministry of Education, Youth and Sports)

Operational Programme Education (Ministry of Education, Youth and Sports)

IOP – Integrated Operational Programme (Ministry for Regional Development)

Operational Programmes Cross-border Co-operation for Objective 3 European Territorial Co-operation

Operational Programmes Transnational and Interregional Co-operation for Objective 3 European Territorial Co-operation (2007-2013)

Single Programming Document Objective 2 of NUTS II region, the Capital City of Prague for 2004-2006 (Ministry for Regional Development of the Czech Republic in co-operation with the Prague City Council)

Methodology for Financial Flows and Control of the EU funds and the Cohesion Fund (Ministry of Finance)

**Acts and regulations in force in the Czech Republic, with special regard to:**

Act No. 513/1991 Coll., Commercial Code

Act No. 218/2000 Coll., on budgetary rules, as amended

Act No. 250/2000 Coll., on budgetary rules applying to territorial budgets, as amended

Act No. 219/2000 Coll., on property of the Czech Republic and acting of the State in legal relations, as amended

Act No. 40/2004 Coll., on public procurement, as amended

Public Procurement Bill – Document for discussion at the sitting No. 1076

Concession Agreements and Concession Procedures Bill – Document for discussion at the sitting No. 1078

### **Guidance materials of the PPP Centrum Czech Republic**

EU Funds and PPP Guide book – PPP Centrum material

Approach to PPP risk management – PPP Centrum material

Introducing PPP – PPP Centrum material

### **Other relevant documents**

Progress schedule of programming documents preparation for the programming period 2007-2013 (Government of the Czech Republic)

Status of Steering and Coordinating Committee for the purposes of coordination of support provided in the programming period 2007-2013 by the European Communities at the national level (Government of the Czech Republic)

Rules of Procedure of Steering and Coordinating Committee for the purposes of coordination of support provided in the programming period 2007-2013 by the European Communities at the national level (Government of the Czech Republic)

Czech Government Resolution No. 245 of 2 March, 2005 on the progress of preparations of the Czech Republic for drawing on the EU funds and the Cohesion Fund for 2007-2013 (Government of the Czech Republic)

PPP Hybrid financing structures: Leveraging EU funds and private capital (Draft Final Report for the World Bank) (PwC)

Developing Public-Private Partnerships in New Europe (PwC)

AIRCON Case study of PPP project and EU funds combination (Johnson & Kramařík)

Study of PPP application for funding of a transport project under the EU Fund (Johnson & Kramařík)

The impact of TENs co-financing and subsidy conditions on projects, and proposals for reform (Dutch Ministry of Finance) – KPMG

Commission interpretative communication on concessions under Community Law (2000/C 121/02) (Official Journal of the European Communities)

GUIDANCE ON THE METHODOLOGY FOR CARRYING OUT THE COST-BENEFIT ANALYSIS Information note n° 64 (Fiche No. 64)

Guidelines for Successful Public-Private Partnerships (European Commission)

Resource book on PPP case studies (European Commission)

State aid under the EU law

Eligible expenditure – methodological guideline (Ministry for Regional Development)

JASPERS: A New Technical Assistance Partnership

JASPERS – WORKSHOP IN DG REGIO HELD ON 09/12/2005 (9:30 a.m.-2:00 p.m.)

**Final Report on Project 1p/05 – “Application of the PPP Principle on the Economic and Social Cohesion Policy” dated 15 May, 2006**

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