

Public/Private Cooperation in the Ports Sector – A Best Practice Note

Establishing the Right Regulatory Framework for your Port

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1. INTRODUCTION

The success of any public/private cooperation with respect to ports depends ultimately on the quality and efficiency of the cooperative interaction. The paramount task that the State has is to establish the necessary basic conditions by regulating key areas reliably and consistently whilst giving the cooperating parties (the relevant public authority and the private partner) the flexibility to take into account the unique circumstances of a particular project. Individual countries meet these requirements in different ways and with varying degrees of success for their country.

The purpose of this note is set out the best practice for establishing a regulatory framework that facilitates and maximises the outcomes of public / private cooperation. In this note we: (i) examine the types of port functions amenable to cooperation; (ii) highlight some of the major models of public / private cooperation; (iii) examine the key elements for a successful legal and regulatory regime; and finally (iv) make some recommendations for the establishment of the right regulatory framework.

2. PORT FUNCTIONS

The operation and administration of a port include the provision of nautical services as well as numerous other responsibilities. Whilst a number of these functions are well suited to a form of privatisation some of them will be excluded from privatisation due to their sovereign nature.

a) Genuinely Sovereign Functions

Sovereign tasks and functions include:

- ▷ *Planning and Development of Ports* - strategies are developed with the aim of advantageously positioning a State's ports in international competition.
- ▷ *Award of Permits* - for instance for the construction of port facilities or for port use.

- ▷ *Operation of National Sovereign Services* - such as customs, police, military, etc.

b) Landlord Functions

In the vast majority of jurisdictions the State, as the owner of the port area, exercises landlord functions. Landlord tasks typically encompass the letting of some or all of the port area and facilities as well as the award of leases/concessions.

It is important to distinguish between the ownership position of the State with regard to port land and fixed facilities / equipment and the actual *operation* of a port, this latter role is increasingly being ‘outsourced’ to private service providers.

c) Provision and Operation of Infrastructure and Superstructure

The infrastructure of a port consists primarily of the waterways, road and (partly) rail networks in the port as well as road and rail connections to the ‘hinterland’. The superstructure consists of warehouses, office buildings, or fixed facilities / equipment (such as container gantry cranes or loading plants) as well as some parts of the port railway system (incl. track switches, terminals, etc.).

Whilst the public authorities often provide and maintain the infrastructure, they increasingly rely on the know-how of private partners when it comes to the superstructure.

d) Nautical Services

Nautical services include:

- ▷ *Organization, Control and Monitoring of Shipping Traffic.*
- ▷ *Pilotage, Towage and Mooring.*

The former tasks are traditionally taken over by the port authorities whilst pilotage, towing and mooring is increasingly being provided by private partners that remain subject to a certain State supervision (particularly where relevant in terms of security).

e) Other Services

Important port functions are of course cargo handling and storage as well as other port related services, these are usually not covered by the State but managed by private partners.

f) Imposition of Charges

Ship owners are charged fees and tariffs for all manner of services when their ships call at port.

A distinction can be drawn between: (i) *port tariffs* that are charged by the public authorities for the use of the port and the infrastructure as public goods; (ii) and *service fees* that are charged by private service companies for specific services provided on a contractual basis.

Charges are still frequently raised by the public authorities and the relevant private service companies individually.

3. POTENTIAL MODELS OF COOPERATION

Public/private cooperation can be conducted on the basis of a number of main models illustrated below:

- ▷ Joint-Ventures;
- ▷ Transfer of Property;
- ▷ Leases;
- ▷ Concessions.

In practice cooperation within a port virtually never takes place pursuant to only one model, the parties generally deploy hybrid forms tailored to the concrete project at hand.

a) Joint Ventures

The joint venture model describes a structure in which both the private partner and the public authorities participate directly in the same company.

An important factor in this scenario is to appropriately allocate decision-making competence as well as liability. Hence the choice of the suitable corporate form is relevant to the cooperative endeavour.¹ The final decision will depend on the particular circumstances of the individual project, i.e. the project risk potential and/or the need for powerful control instruments on the part of the public authorities.²

In an ideal world, the joint venture model, facilitates that the State and the private partner work particularly closely and in a complementary manner by focussing on their respective areas of expertise. However, if not managed properly there is a risk of this potential benefit turning into a disadvantage, i.e. when decision-making processes are delayed by way of an imprecise and/or inappropriate allocation of the business plan. Further, the mutual reliance of the partners on each other is of particular importance with this form of cooperation, since they each depend on the other's respective contributions to a greater extent than would otherwise be the case under other models of cooperation.

It is for these reasons that in practice joint ventures between public and private parties are relatively uncommon in the ports sector.

¹ Cf UNCTAD-Secretariat, Guidelines for Port Authorities and Governments on the privatization of port facilities, 1998, S. 12, available at <https://unctad.org/en/Docs/posdtetibd1.pdf>, last visited on 23 May 2019.

² Cf. Schede/Pohlmann, in: Praxishandbuch Public Private Partnership, 1. Edition, 2006, p. 150 et seq.

While too low an inclusion of the private partner's capital may adversely affect his performance incentives, requirements that are too onerous will have a deterrent effect. Similarly, the lease term should be set for a length of time that furthers the stability and continuity of the port operations with options to review the competitiveness of the private partner's offer after a certain period of time. The lease instalments should be adjusted to the financial commitment of the private partner, allowing him to re-coup his expenses and earn a reasonable return.⁶

The lease model has become a common and acknowledged mode of port privatisation.⁷

d) Concessions

Under this model, as with the lease model the private partner is granted the right to use certain port land and/or fixed facilities / equipment for a specified period of time. In contrast to the lease model additional economic risks are imposed on the private partner. In addition to the operation of the superstructure and the port facilities, the private partner assumes full responsibility for the funding of the project.⁸ Internationally the distinction between concession and lease is drawn inconsistently. The English term "concession" is often used to include the lease model.⁹

There are a variety of different subtypes to the concession model.¹⁰ The parties may agree that the State retains or later acquires ownership of the relevant port facilities or alternatively specify that relevant port facilities are owned and retained by the private partner, the terminology commonly used is as follows:

- ▷ Build-Operate-Transfer (BOT);
- ▷ Build-Own-Operate (BOO); and
- ▷ Build-Own-Operate-Transfer (BOOT).¹¹

The scope of services that can be subject to a concession agreement range from the provision of some or all of the superstructure to dredging and land reclamation. Concession agreements regularly have

⁶ UNCTAD Secretariat, Guidelines for Port Authorities and Governments on the privatization of port facilities, 1998, p. 8 et seq., available at: <https://unctad.org/en/Docs/posdtetibd1.pdf>, last visited on 23 May 2019.

⁷ The World Bank, Port Reform Toolkit, 2. Edition, 2007, p. 111 et seq., available at: http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/documents/toolkits/Portoolkit/Toolkit/download_modules.html, last visited on 23 May 2019; UNCTAD secretariat, Guidelines for Port Authorities and Governments on the privatization of port facilities, 1998, p. 9, available at: <https://unctad.org/en/Docs/posdtetibd1.pdf>, last visited on 23 May 2019.

⁸ The World Bank, Port Reform Toolkit, 2. Edition, 2007, p. 112 ., available at: http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/documents/toolkits/Portoolkit/Toolkit/download_modules.html, last visited on 23 May 2019.

⁹ The World Bank, Port Reform Toolkit, 2. Edition, 2007, p. 112 ., available at: http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/documents/toolkits/Portoolkit/Toolkit/download_modules.html, last visited on 23 May 2019.

¹⁰ The World Bank, Port Reform Toolkit, 2. Edition, 2007, p. 117 et seq., available at: http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/documents/toolkits/Portoolkit/Toolkit/download_modules.html, last visited on 23 May 2019.

¹¹ UNCTAD Secretariat, Guidelines for Port Authorities and Governments on the privatization of port facilities, 1998, p. 10 et seq., available at: <https://unctad.org/en/Docs/posdtetibd1.pdf>, last visited on 23 May 2019.

long terms of up to 40 years due to the high investment expenses of the concessionaire as well as the depreciation periods of the fixed facilities / equipment.

A potential disadvantage of the concession model from the point of view of the State is the possibility that the State may have little influence on the quality of the maintenance measures performed by the concessionaire. On the other hand, the private partner will be wary of a too prominent role envisaged for the public authorities. When determining the terms of the concession agreement attention must be given to the objective that a generally very prominent role of the public authorities does not conflict with the implementation of efficient business structures.¹²

The concession model offers great opportunities to benefit from the innovation potential of private partner, it is therefore widely accepted and commonly made use of in ports around the world.

4. KEY ELEMENTS OF A SUCCESSFUL REGULATORY REGIME

The necessary requirements for a regulatory regime for port privatisation naturally differ depending on perspective (State or private partner). For the State concerned it is of great importance to establish a competitive ports system from whose successful business it will (directly and/or indirectly) benefit. Port customers expect a non-discriminatory access to ports and a single point of contact for all port-related administrative matters (a "one-stop-shop" solution). Further, in the interests of fostering competition, free access (at least to minimum volumes) should be considered.

From the perspective of private partner, a port privatisation project is only attractive when it takes place in a regulatory system that meets certain fundamental criteria. These criteria include both the *transparency* of the relevant rules and procedures as well as *flexibility* for the private partner concerning operational procedures and reimbursement. Further, the rights and duties of the parties involved in the port operation must be allocated unambiguously.

a) Transparency and Coherence

"Transparency" in this sense means above all a clear structure of the regulatory framework. In order to achieve this goal the sector-specific rules should be consolidated in as few statutes as possible. It is also important that the regulatory regime meets the requirements of all ports within a State (be they large commercial ports or smaller ports).

There must be a clear separation between: (i) the service functions relating to the operation of a port; and (ii) the administrative functions of the relevant port authority. A transparent regulatory regime

¹² UNCTAD Secretariat, Guidelines for Port Authorities and Governments on the privatization of port facilities, 1998, p. 11, available at: <https://unctad.org/en/Docs/posdtetibd1.pdf>, last visited on 23 May 2019.

should focus on the distinct distribution of administrative functions within the administrative machinery and regulate to ensure the cooperation of the relevant authorities.

Transparency also means ensuring non-discriminatory negotiations and contracts between the public authorities and their potential private partners.¹³ Similarly, all port fees including public dues should be broken down and charged based on clear and comprehensible criteria.¹⁴ Appropriate procedures must be established for the purpose of determining compliance with these requirements.¹⁵

Finally, the State should make information available on the funding that it provides its ports.¹⁶

b) Clear Allocation of Tasks, Rights, and Duties

The applicable set of rules must guarantee a basic allocation of tasks, rights and duties of the parties involved in order to allow for the orderly cooperation of all. In addition, the fixed distribution of responsibilities should apply to all ports equally so as to administer them efficiently. It is unfortunately not uncommon to find that the authorities involved in the administration of a port and each of their respective competences vary even between the different ports in one State. Such inconsistent and scattered distribution of tasks considerably aggravates and retards the development and implementation of a national ports strategy. Moreover, port customers have to rely on a variety of authorities that in the worst case reach contradictory decisions. This confusion of responsibilities not only deters private partners, but also significantly limits the possibilities of exchange of experience between port authorities.

A clear-cut and efficient division of responsibilities should be established by clearly and consistently splitting up licensing and legal supervision competences between a Central Administrative Authority and Regional Port Authorities. (Please refer to Section 5 for an allocation of responsibilities between the Central Administrative Authority and Regional Port Authorities).

c) Flexible Arrangements – Operational Procedures and Remuneration

The tasks that public and private partners have to accomplish will not just differ from State to State but also from port to port. It is for this reason the specific operations and the remuneration of private partners cannot reasonably be exhaustively regulated by statutory law. The details of a cooperation between the State and their private partners can be negotiated and determined much more effectively by the actual parties to a particular project.

¹³ Commission of the European Communities, Communication on a European Ports Policy, COM (2007) 616 final, p. 9 et seq.

¹⁴ Commission of the European Communities, Communication on a European Ports Policy, COM (2007) 616 final, p. 12.

¹⁵ Case C-324/98 *Telaustria v Telefonadress* [2000] ECR I-10745 Recitals 60, 62; Case C-458/03 *Parking Brixen v Gemeinde Brixen* [2005] ECR I-08585, Recital 49.

¹⁶ Commission of the European Communities, Communication on a European Ports Policy, COM (2007) 616 final, p. 9.

The overall framework and basic principles should be determined by statutory law, e.g. concerning possible modes of reimbursement and procedures for review and intervention. The effective remuneration the private partner receives should be based on the performance he delivers in relation to the concrete project. In particular, the private partner must be given the opportunity to respond to rising costs and expenses on his part with a corresponding adjustment of his consideration. In return, profit-sharing could be an option for the State.

Pricing by a private enterprise is a controversial issue, especially in countries where fees are traditionally determined by the State. Usually, the avoidance of discriminatory pricing and the prevention of monopolies are stated as reasons for a price control. It is also argued that price control prevents a reduction in service quality to a level that could cause a public safety hazard due to exceedingly intense competition. Having said that, there are strong arguments in favour of granting the private partner pricing autonomy. Among these are the greater probability that cost based tariffs will apply and that these will likely ensure that the costs and expenses incurred will be financed out of the actual operating turnover. In addition, the introduction of an efficient pricing system means that each customer pays a fee that corresponds with the services he has made use of, in other words a greater price equality. Finally, the prices should reflect the real benefits of the service offered to customers to a larger extent.¹⁷

The manner in which the private partner executes the tasks conferred on him should be for him to decide so that the desired efficiency gains and innovation potential can be fully utilised.¹⁸ It is not advisable to attempt to regulate every detail with regard to the performance of the private partner, but rather to stipulate output specifications against which the quality of work is measured.¹⁹

5. ESTABLISHING THE RIGHT REGULATORY FRAMEWORK

a) Groundwork

The legal and regulatory framework is not only comprised by the sector-specific requirements. Consideration must also be given to applicable provisions of Constitutional, Public Procurement, Anti-trust, State Aid, Employment, Investor Protection, and/or General Administrative Law.

¹⁷ UNCTAD Secretariat, Guidelines for Port Authorities and Governments on the privatization of port facilities, 1998, p. 17, available at: <https://unctad.org/en/Docs/posdtetibd1.pdf>, last visited on 23 May 2019.

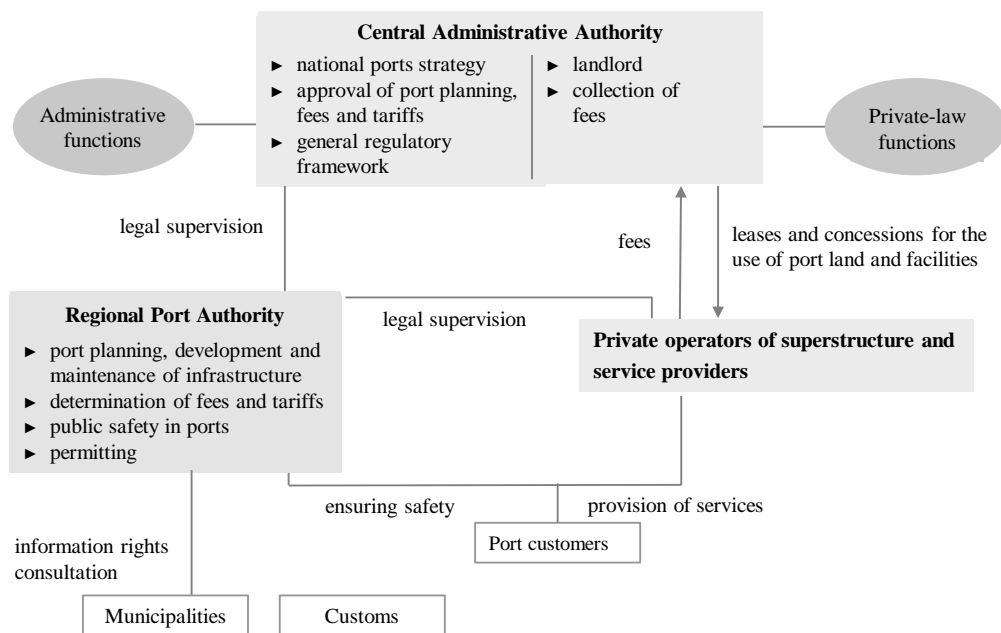
¹⁸ The World Bank, Port Reform Toolkit, 2. Edition, 2007, p. 117, available at: http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/documents/toolkits/Portoolkit/Toolkit/download_modules.html, last visited on 23 May 2019.

¹⁹ Alfen/Fischer, in: Praxishandbuch Public Private Partnership, 1. Edition, 2006, p. 25

As a first step the relevant rules in these areas of law will need to be identified and reviewed so as to ensure these fully permit an envisaged regulatory regime. If the result is negative, remedial measures supporting the creation of an attractive regime should be considered and implemented.

As previously stated, a successful regulatory regime must be transparent and show a sufficient degree of flexibility to allow the parties to take account of the individual circumstances of a project. There are two vital prerequisites for a regulatory framework to achieve these characteristics: (i) a clear distinction should be drawn between *port operation* and *port administration*; and (ii) the sovereign (administrative) functions of the State and potential actions taken on the basis of civil law should be clearly separated.²⁰

The following diagram below sets out an efficient regulatory framework.



b) Central Control

In view of the administrative functions of the public authorities it is advisable to combine local expertise and centralized control in the form that administrative powers are divided between one Cen-

²⁰ The World Bank, Port Reform Toolkit, 2. Edition, 2007, p. 114, available at: http://www.ppiaf.org/ppiaf/sites/ppiaf.org/files/documents/toolkits/Portoolkit/Toolkit/download_modules.html, last visited on 23 May 2019.

tral Administrative Authority at State level and several Regional Port Authorities. The Central Administrative Authority should broadly be responsible for the national ports strategy, the approval of port planning, approval of fees and tariffs, award of concessions, landlord functions, the collection of fees, legal supervision of the port authorities, and the regulatory framework as a whole.

The civil law functions of the public authorities, in particular the letting of public properties, should be taken over by a Central Administrative Authority to guarantee uniform and clear standards concerning the contracts. It should also be the responsibility of this administrative authority to grant concessions and conclude lease contracts with private partner.

c) Local Expertise

The Regional Port Authorities should be responsible for port planning and development, determination of fees and tariffs, public safety, and permitting. Thereby a coherent regulatory framework is established which can be adapted to local requirements by the Regional Port Authorities.

The Regional Port Authorities should, as an extension of the Central Administrative Authority, assume the responsibilities of port planning and port development at the local level. The latter includes the provision and maintenance of port infrastructure. Apart from the remuneration of the private partner, which is best left to individual contractual agreements, they also set the public charges for the use of their ports. Further, due to local geographical conditions, among other reasons, the Regional Port Authorities are in the best position to ensure public safety, both in terms of operations on the port grounds and in terms of navigation (port master).

In order to realise the previously mentioned "one-stop-shop" solution, the award of permits for public use of the port should be concentrated at the relevant Regional Port Authority.²¹ In cases where such a transfer of such administrative powers is not feasible, the Regional Port Authorities should at least act as a focal point for port customers and coordinate the administrative proceedings. Similarly, the establishment of a body which vessel owners can pay all fees and charges to would facilitate this procedure considerably.²² For the purpose of separating port operation and port administration it is essential that the Regional Port Authorities provide no services other than those imperatively necessary to ensure public safety.

It is strongly advised to include the Regional Port Authorities in the management of the port estates as well as the contract realisation.

²¹ Cf. UNCTAD secretariat, Guidelines for Port Authorities and Governments on the privatization of port facilities, 1998, p. 15 et seq., available at: <https://unctad.org/en/Docs/posdtetibd1.pdf>, last visited on 23 May 2019.

²² Commission of the European Communities, Communication on a European Ports Policy, COM (2007) 616 final, p. 12.

6. CONCLUSION

If executed correctly and including the right balance of incentives and certainty in the form of a comprehensive, transparent, and flexible regulatory regime, a country can profit greatly from public / private partnerships in the ports sector.

A further form of cooperation being successfully implemented in Europe, over and above the widely spread lease/concession model for the operation of a port, is the transfer of the maintenance obligations of superstructure to private partner. In addition, in many major European ports, the sea-side nautical services (pilotage, towage and mooring) are more and more often provided under civil law contracts. The relevant port authorities merely assume a supervisory role in these cases. The increasing privatisation of cargo handling and storage in Europe has led directly to the introduction of advanced technologies and thus to substantial efficiency gains.²³

Many States will – not least in view of tightening budgetary situations – increasingly need to depend on the support of private partners for efficient and successful port operations. In order to master the associated challenges and successfully exploit market efficiencies and innovation potential, a transparent, structured and efficient regulatory regime is the absolute fundamental prerequisite.

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²³ Commission of the European Communities, Communication on a European Ports Policy, COM (2007) 616 final, p. 11.