



Analysis on Public-Private Partnership Bosnia and Herzegovina



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This document has been produced as a part of the project “CSOs as equal partners in the monitoring of public finance“ which started beginning of 2016 and is implemented by a consortium of 10 organizations from 7 countries and will last for four years.

The aim of the project is to improve the transparency and accountability of policy and decision making in the area of public finances through strengthening the role and voice of NGOs in monitoring the institutions that operate in the area of public finances. In this way, the project will strengthen CSO knowledge of public finance and IFIs and improve CSO capacities for monitoring. Additionally, it will help advocate for transparency, accountability and effectiveness from public institutions in public finance. Moreover, this project will build know-how in advocating for sustainability, transparency and accountability of public finance and IFIs. This project will also increase networking and cooperation of CSOs on monitoring of public finance at regional and EU level. Lastly, it will increase the understanding of the media and wider public of the challenges in public finance and the impacts of IFIs.

Key project activities are research and monitoring, advocacy, capacity building and transfer of knowledge/practices and networking in the field of the 4 specific topics: public debt, public-private partnerships, tax justice and public infrastructure.

More information about the project can be found on <http://wings-of-hope.ba/balkan-monitoring-public-finance/> and on the Facebook Page Balkan Monitoring Public Finances





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INTRODUCTION

As the Public Private Partnerships (PPPs) is a model of financing which BiH's government very much consider as one of the possibilities that could be used in order to provide and improve much needed services or infrastructure projects for the citizens, this study looks into current challenges focusing on policy and legislative framework, institutional capacities and external factors, such as PPP awareness. The study recommendations involve clear formulation of PPP policy, followed by the legislative framework and enhanced institutional capacities, monitoring of PPPs as well as recommendations for raising general level of understanding of PPPs.

Bosnia and Herzegovina (BiH) has been confronted with serious fiscal constraints and given the increase in the levels of public debt, will continue to be so even on the larger scale in the upcoming years. Private sector engagement has been obtained through public-private partnerships (PPPs) which is a long-term cooperation between public authorities and the world of business set by the agreement for realization of the PPP projects. Despite concerns over the effectiveness of some forms of PPP, especially their value for money and financial sustainability, PPPs are increasingly seen as an acceptable option.

Since in FBiH alone there is over 9,6 billion KM in public capital that could be privatized or partnered up with the private sector (42% of it, or 4 billion KM, is located in the energy/water/ gas sector; 21%, or 2 billion KM, is placed in the infrastructure sector), the potential for PPPs is obvious.¹ However, implementing PPPs is a difficult task, especially for a country like BiH with complicated political situation, conflicting local interests, corruption schemes and lack of institutional capacities and understanding of PPP. Therefore, in order to rightfully implement PPP projects, a clear PPP policy must be formulated, supported by a comprehensive legislative framework and coupled with adequate institutional capacities.

¹ Grim(m) Fairytale of Public Private Partnerships in Bosnia and Herzegovina - Focus on the Healthcare Sector, Nađa-Azra Uzunović i Zana Karkin



1. UNDERSTANDING PPPS IN BOSNIA AND HERZEGOVINA

Public-Private Partnership is a model of long-term contractual relations between the public and the private sector; it can relate to the provision of financing, project design, construction, management and/or maintenance of infrastructure and/or service provision on behalf of the private sector, traditionally purchased and provided by the public sector. The basic idea of Public-Private Partnership is to link, whenever possible, the risk sharing between the public and the private sector on the one hand with a higher efficiency in project implementation, to be provided by the private sector, on the other hand. Considering the poor state of public services provision in many low- and middle-income countries, such as BiH, the PPP is increasingly seen as a way of solving the problem of insufficient financial resources with simultaneous increase of service quality.

Legal regulation in this area is very complicated in BiH. There are 12 laws on PPP and 14 laws on concession. The political administrative environment is such that in BiH there is no unified Law on PPP. While one entity, Republic of Srpska, has adopted Law on PPP in 2009, the other entity, Federation of B&H, has drafted Law on PPP in 2009 and it is still in adoption process. PPP projects cannot be carried out on state level because it is not regulated by the constitutional framework, and there would be political resilience in this situation.

The concession model is a frequently applied contractual form of PPP in BiH. It features a direct link between the private partner and the beneficiary. The private partner provides services to the users instead of the public partner but under the supervision of public partner. The income of the concessionaire (private partner) consists of charged service fees, and if so agreed, additional subsidies from the public sector. Laws on concessions in Bosnia and Herzegovina regulate the modalities and conditions related to the award of concessions, including the competence and institutional structure of the Commission for the concession, tender procedure, the contents of the concession contracts, the rights and obligations of the concessionaire. Referring to the object of concession, the usual division of concessions is for exploitation of natural resources (goods in general use - infrastructure) and concessions for the provision of public services. In order to enter the realization of any concession project it is necessary to perform a feasibility study. According to the legislation, this study is performed by the grantor (the public sector), and for unsolicited offer, feasibility study can be requested from potential concessionaires (private sector).²

² Javno - privatno partnerstvo kao instrument unapređenja javnih usluga na lokalnom nivou, MDP, November 2009



Previous experiences in BiH show that the very large number of concession and public-private partnership contracts are awarded via unsolicited offer, without sufficiently open, transparent and competitive procedures. Using the unsolicited proposal means that the grantor is not in a position to assess whether the concession (based on unsolicited proposal) is the best offer in technical and economic terms. The lack of an open and competitive procedure means that a possibility of inviting additional potential candidates and broadening the basis for competition is missing. This, in return, leads to the absence of real competition in prices, because the bidders are under less pressure to offer greater value for money, in terms of the concession fee as well as product quality. The end result is that the revenue from the concession fee is likely to be lower, and the final users will not necessarily get the best value for money.³

The other model of PPP is *institutional model*. The main characteristic of PPP is the establishment of common institution of public and private sector in order to implement certain public project or provide public services. The institutional forms of PPP are recommended for the provision of public services that are of great importance for the public sector which is why it is necessary that the public sector retains part of the control and oversight over the provision of services (eg. air traffic control, water supply, etc.). Law on PPP also envisaged the establishment of a company for the individual projects. It is a company of capital that is established for the sole purpose of implementing PPP projects. For the selection of the private partner, local community carry out a public procurement procedure in accordance with the criteria (quality of service, the lowest price, functionality, and other elements) that are required by the Law on PPP of RS and the Law on Public Procurement.⁴

Not a lot can be said about PPP Contracts signed in BiH, simply because they are not available to the general public. There is no precise record on number of applications nor registers of awarded concessions. Besides, recording and charging of concessions fees, as well as oversight are not satisfactory. For example, it was not possible to provide a number of applications in recent years, nor the number of initiated and unfinished procedures for the award of concessions. There are no available data on how many requests for concessions were submitted annually or announced public calls. Not a single institution has a record on how many concessions were awarded on the level of cantons and

³ Strukovni pregled Koncesije i javno-privatna partnerstva u Bosni i Hercegovini, Final report, SIGMA, November 2008/September 2009.

⁴Javno - privatno partnerstvo kao instrument unapređenja javnih usluga na lokalnom nivou, MDP, November 2009



municipalities and from which areas, or how many of them are implemented and what are the effects that have been achieved in management of concessions.⁵

However, considering the poor institutional capacities of both entities regarding the PPP, poorly negotiated contractual arrangements, the miscalculation of project risks by the private sector, corruption or incompetence, or political interference can be expected.

1.1. Analysis of relationship between PPP and Infrastructure

The PPP concept is very undeveloped in BiH, but the role of the private sector in financing of infrastructure is explicitly emphasized in the actual Development Strategy of BiH. BiH governments have begun to consider the use of the PPP model to attract private finance because of budgetary constraints preventing them to take the desired investments and achieve the optimal level of infrastructure. They chose this path because, among many reasons, they are restrained by the lack of possibility of increasing public debt beyond certain limits. An important reason for the introduction of PPP is intention to finance infrastructure from non-fiscal sources. There is an expectation that PPP can contribute to the closure of financial gap based on financing of infrastructure from private sources. However, participation of private investors in infrastructure projects depends on many factors, which in the case of BiH can be reduced to political, regulatory and commercial risks.

1.2. Research on Infrastructure-related PPPs

The FBiH government is currently considering a Public-Private Partnership ('PPP') concession for the Karuse - Poprikuse section of Corridor Vc which has been prepared with the assistance of the IFC Advisory. The EBRD is interested to consider providing further support for developing this PPP.⁶

The involvement of the IFIs in any PPP process would help to ensure the transparency of the tender procedure, however there are other reasons for concern. If a toll is charged on the relevant sections the concessionaire's income will be dependent on the volume of traffic, and experience in many central and

⁵ Izvješće revizije učinka, Upravljanje koncesijama u Federaciji Bosne i Hercegovine, Ured za reviziju institucija u FBiH Sarajevo, February 2011

⁶ <http://www.ebrd.com/work-with-us/projects/psd/corridor-vc-2.html>



eastern European countries has proven that it is extremely difficult to predict the level of traffic. This has led to either concessionaires obtaining guarantees from the state that it will top up their income if it is less than expected, or to arrangements involving availability fees, in which the state pays the concessionaire rather than the motorway users doing so. Either way, after the construction is finished there is almost no risk transferred to the private sector, as the operation of a motorway is not an especially complex matter so performance targets are not difficult to fulfil.⁷

In addition, the Republic of Srpska has given two concessions to foreign investors (Chinese companies) for construction of new thermal power plants: Stanari with capacity of 300 MWh and Ugljevik 3 with capacity of 2x300 MWh.

1.3. Analysis between PPP and debt

Although there is urgent need to improve public policies and legal framework, and strengthen institutional capacities in both entities and in cantons, it is still very unlikely that it will solve the biggest problem of PPP – accumulation of off-balance sheet debts and inability to truly transfer risk to the private sector when the basic public services are in question.

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Hundreds of millions of marks debt of institutions in FBiH have prompted the relevant ministries to think about possible solutions to this problem. Given the financial constraints of the country's budget, PPPs are popping up as one of the possibilities which the government could use in order to provide and improve much needed services for the citizens.

⁷ Report from fact-finding mission on Corridor Vc motorway, Bosnia and Herzegovina, 23 - 25 February 2010



1.4. Cases of PPPs causing debt

60% of all PPP projects in Republic of Srpska so far have been in the health sector - dialysis and radiotherapy. The following projects have been implemented based on PPP with the company International Dialysis Center: construction and equipping of a Hemodialysis Center Laktasi, a Hemodialysis Center Eastern Sarajevo – Kasindo, and a Hemodialysis Center Banja Luka. The following projects have been implemented based on PPP with the Frensis Medical Care: construction and equipping of Hemodialysis Center Samac, Hemodialysis Center Dobož, Hemodialysis Center Zvornik, Hemodialysis Center Prijedor and Hemodialysis Center Gradiska. Based on PPP, the construction is currently ongoing of Hemodialysis Center Foca.⁸

It is true that dialysis through PPP is performed in newly-renovated and newly-equipped rooms, leading to increased satisfaction of patients, but at what price? Dialysis patients in Republic of Srpska raised their concern over many things related to these arrangements. Among other things, the monitoring done by the public partner was not objective and the provisions are higher than in FBiH. According to the data of the RS Health Insurance Fund, EUR 110 is fixed price of chemo dialysis in RS, and more complexed chemo dialysis is EUR 130, while according to a public partner in FBiH the provisions for chemo dialysis services cost about EUR 85. Patients also expressed that one of the biggest weaknesses of PPP arrangements is that, through the legislative framework, the end users are not in any way consulted when it comes to the monitoring and evaluation process of service provision.⁹

Radiotherapy Center Banja Luka has been built based on PPP with the company Euromedic Diagnostic Holland. This Contract was signed for the duration of 15 years and the total investment by the private partner amounted to EUR 20 million, which included building a total of four new floors of the medical ward at the Clinical Center in Banja Luka, bringing radiotherapy specialists from neighboring countries who would transfer the know-how and skills to the local staff, and partnering with Methodist International in Houston, Texas as a quality assurance.¹⁰ Not a lot can be said about PPP Contracts signed in RS because they are not available to the general public.

⁸ <http://www.investsrpska.net/index.aspx?PageID=377&menuID=374>

⁹ Bajka o javno-privatnim partnerstvima u Bosni i Hercegovini - analiza sektora zdravstva, Nadja-Azra Uzunović i Zana Karkin

¹⁰ Grim(m) Fairytale of Public Private Partnerships in Bosnia and Herzegovina - Focus on the Healthcare Sector, Nađa-Azra Uzunović i Zana Karkin:



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Health institutions in FBiH have millions of marks debt and the relevant ministries are now considering PPP as one possible solution to this problem. It is expected that in a few years, the FBiH will also have PPP projects in health sector, as well as in some other sectors.

There is no information on the exact number of concessions granted but none has been granted at the level of Bosnia and Herzegovina.

At the level of the Federation of Bosnia and Herzegovina, only one concession has been granted, ie the existing concession has been renewed - Blue Water in Travnik.





2. LEGAL AND POLICY FRAMEWORK OF PPPS

2.1. Analysis of legal and policy framework of PPPs

There is no PPP strategy on any level in BiH, nor is there a state-level PPP framework, while the two entities have very different PPP legislation. In line with several layers of BiH public administration, the laws that govern PPP establishment and management in Bosnia and Herzegovina are as follows: the 2004 Law on Public Procurement (“Official Gazette of BiH”, no. 49/04), the 2009 Law on PPPs of RS (“Official Gazette of RS”, no. 59/09), the 2007 Law on PPPs of Brčko District (“Official Gazette of BD”, no. 7/10), the 2002 Law on Concessions of BiH (“Official Gazette of BiH”, no. 32/02), the 2002 Law on Concessions of FBiH (“Official Gazette of FBiH”, no. 40/02), the 2002 Law on Concessions of RS (“Official Gazette of RS”, no. 25/02), the Guidebook on PPPs in RS (“Official Gazette of RS”, no. 104/09), the Law on Concessions of Brčko District (“Official Gazette of BD”, no. 41/06), as well as cantonal laws on concessions and cantonal laws on PPPs.

Republic of Srpska has adopted the Law on PPPs of RS (“Official Gazette of RS”, no. 59/09), and introduced its amendments in 2011, but its weakest link remains the monitoring and risk sharing provisions. FBiH has had a draft version of the Law on PPPs since 2009, and is now awaiting public hearing. On the other hand, 8 out of 10 cantons have already adopted PPP laws, mainly through ministries of finance or economy. The oversight over PPP projects should be conducted by the relevant Commissions for Concession. BiH has three regulatory commissions for concession: Commission for Concession of BiH, Commission for Concession of RS and Commission for Concession of FBiH. In addition, in some cantons we have cantonal commissions for concession.¹¹ The existence of several similar, yet separate legal regimes for concessions/PPPs in the country, as well as their inevitable overlap, thus discourages cross-entity and inter-entity concessions/PPPs.

Considering that entities and cantons have adopted or drafted PPP laws, and given the fact that public private partnerships are very much linked to the public procurement as well as the concessions field, it is also important to consider PPP legislation at the state level in order to have a harmonized legal structure for avoiding overlaps, inconsistencies and loopholes and to ease future interactions with the EU-level financial institutions. But, considering the current political situation, forecast that law on the state level will be adopted cannot be optimistic.

¹¹ Iskustva BiH u JPP i koncesijama, presentation of Milomir Amovic



In BiH there is no national, dedicated PPP agency to promote and develop projects, though each entity has its own commission for concessions, but no official body for PPPs. Institutional responsibilities are not sufficiently defined, and the commissions and line ministries involved in project planning and oversight do not possess the necessary technical expertise on project financing, risk evaluation and contract design. In RS, within the Ministry of Finance, the Public Investment Department oversees PPP projects, but there is no official department nor are there employees with job descriptions which focus on PPPs alone. Draft FBiH Law on PPPs stipulates transferring PPP responsibility to the Commissions for Concessions on the federal/cantonal level. Even though Commissions are staffed with highly educated employees, taking into consideration the current implementation of concessions, it is unlikely that PPP implementation would go much differently.¹²

2.2. Analysis on relationship between stakeholders, and who are the actors pushing for PPPs.

The governmental institutions from both entities recognized the PPP model as a measure for improvement of BiH economy. They usually present this model as something that would bring many advantages and possibilities to private sector in terms of secured employment, long-term contracts, the possibility of extending the contract, and certainly banks give more support due to low risk of non-payment of loans. It also provides allocation of risks, more efficient project management by using the know-how and methods from the private sector and ultimately it leads to economic growth and provide better services to citizens. But, they often fail to present the risks of the PPP model. PPP is often more expensive than public sector management, of dubious efficiency from the point of the consumer, and actually leads to a transfer of resources from the public to the private sector. In BiH the problem is that the public sector is inefficient because of the political system, and under these circumstances PPP is simply an invitation to further corruption, lack of oversight, and rising charges to consumers.

¹² Grim(m) Fairytale of Public Private Partnerships in Bosnia and Herzegovina - Focus on the Healthcare Sector, Nađa-Azra Uzunović i Zana Karkin



3. PPPS RISKS AND IMPACT IN LOCAL AND NATIONAL LEVEL

3.1. Corruption in PPP

PPPs can provide an opportunity for corruption which is significant in the case of BiH, since the 2016 Transparency International Corruption Perception Index ranked BiH 83rd out of 176 countries. The project selection in general is not based on analysis but corruption or pursuit of political gain tends to dominate project selection. Thus, PPPs in BiH risk getting easily get stuck in a viscous circle of weak institutions, a lack of transparency in deals, obvious conflicts of interest, corruption, etc.

Due to such PPP contracts, key question is assessment and monitoring of PPP. While the RS performs some kind of ad hoc quasi-independent oversight, FBiH and cantons do not conduct almost any monitoring.

3.2. Transparency as a prevention of corruption in PPP

Transparency represents an encouragement for improvement in the management of resources and ensure openness and competitiveness among investors, and provides opportunity for all investors to have information on possible subjects that are given in concession. It also reduces the risk for future investor and reduce the risk for deception and corruption. Although transparency is explicitly favored in laws on PPP/concession, it is still not sufficiently represented. Also noticeable is the fact, as mentioned before, that the laws on concessions permit awarding concessions based on unsolicited proposal, without public tender, which is not in line with good practices and EU directives. Confirmation of the above is related to the conclusion that 35% of concessions was awarded by the tender process, and 65% through unsolicited proposal.¹³ This is confirmed by a report from SIGMA stating that "the basic characteristic of the concession system in BiH is a large number of concession agreements awarded through unsolicited offer, without sufficiently open, transparent and competitive procedures."¹⁴

¹³ Izvješće revizije učinka, Upravljanje koncesijama u Federaciji Bosne i Hercegovine, Ured za reviziju institucija u FBiH Sarajevo, February 2011

¹⁴ Strukovni pregled Koncesije i javno-privatna partnerstva u Bosni i Hercegovini, Final report, SIGMA, November 2008/September 2009.



3.3. Other identified risks

PPPs is a financing model which is very risky for BiH and it requires very strong public governance institutions. However, institutional capacities in BiH are not developed, or not even present in many cases, and there needs to be a serious effort undertaken in order to build up such capacities. If PPPs are to be applied for the benefit of the BiH society, significant efforts need to be devoted to strengthen institutional capacity.

Poor institutional capacity, along with a general lack of in-country knowledge and expertise about the benefits and dangers of PPP arrangements are big obstacles and risks for adequate PPP implementation.



CONCLUSIONS AND RECOMMENDATIONS

It can be concluded that, so far, there is a lack of political willingness to define the PPP policy framework, no strategic decision making for establishing them, no awareness about the relevance of the monitoring of PPPs by the relevant institutions, and there is a lack of institutional capacities and understanding of PPP by the relevant institutions.

Public Private Partnerships in Bosnia and Herzegovina need to be approached very carefully. Dialogue and discussion on PPPs need to be initiated in the country, involving all relevant stakeholders, in order to deepen both the understanding, as well as the ownership of this concept. The PPP policy needs to be clearly formulated, followed by the legislative framework and enhanced institutional capacities. BiH needs to develop a clear PPP Policy and adopt PPP Strategy that will define areas for PPP involvement.

PPP laws needs to be harmonized with laws on public procurement as well as laws on concessions, so that any overlaps or irregularities are avoided. It also needs to be ensured that the public auditor of each entity audits PPPs on an annual basis and that, by law, all PPP contracts and monitoring reports are available and transparent. It is very important to strengthen institutional capacities, which are currently on a very low level.



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