Road PPPs in Turkey

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The Turkish government has embarked on an ambitious program of large landmark projects done as public-private partnerships, and it is especially keen to encourage foreign sponsor and foreign lender participation in these projects.

Turkey is one of the most exciting high growth markets. Over the last two years, it has had the highest real growth in gross domestic product of any OECD country and, by 2018, it is projected to be the world's second fastest growing economy. It faces a substantial and increasing need for roads and other infrastructure. In a number of sectors Turkey does not have an existing track record in public-private partnerships or PPPs, but based on its economic fundamentals, its demand for infrastructure, its government's support for such projects, and its current road PPP program, Turkey is a market with many potential opportunities.

This article describes the road PPP regulatory framework in Turkey.

Statutory Framework

Article 47 of the Turkish constitution allows the use of public-private partnerships. It allows the government to enter contracts with the private sector to carry out certain public services (including undertaking roads PPP projects).

A number of laws apply potentially to road PPP projects. Two key ones are Law no. 3465 of June 2, 1988 regarding the construction, maintenance and operation of highways by entities other than the General Directorate of Highways, and Law no. 3996 of June 13, 1994 regarding the realization of certain infrastructure and public services with the build-operate-transfer model and the related Council of Ministers decree no. 2011/1807 implementing the Law no. 3996. In the 1990s, there were legal challenges to certain parts of this legislative framework, but the challenges are now only of historical relevance.

Law no. 3465, importantly removed the monopoly of the General Directorate of Highways on undertaking road projects.

Law no. 3996 is a "general BOT law" that covers various specified parts of infrastructure and energy sectors. Current greenfield road PPP projects are being developed under Law no. 3996. However, the transfer of operation rights of existing roads is being undertaken pursuant to another statute --

Law no. 4046 relating to privatisations -- as the core of such a transaction is effectively the transfer of the right to operate a road project for a fixed period of time. For instance, the recent US$ 5.7 billion-privatisation of the operating rights of the two Bosphorus bridges and eight motorways was undertaken pursuant to this statute.

Awards

There are three options as to the manner in which greenfield road PPP projects can be awarded. These are sealed bids among all bidders, sealed bids among at least three bidders and a negotiated procedure. The negotiated procedure may only be used if the other options could not work. Nevertheless, in case of large greenfield road PPP projects, the process is likely to be a mixed one of sealed bids and negotiations.

Transfer of operating rights for existing road projects may be awarded by open bid among all bidders or through a negotiated procedure as deemed fit by the government.

A number of parts of the government will be either directly or indirectly involved in any road PPP project. However, the three key government entities that will have a role will be the Supreme Planning Board (that is a committee made up of the prime minister and eight other ministers), the General Directorate of Highways (that is part of the Ministry of Transportation, Maritime Affairs and Communication), and the Under-secretariat of the Treasury. On a day-to-day basis, road PPP projects will be managed by the General Directorate of Highways. The Supreme Planning Board will be involved in a limited number of decisions of fundamental importance. The Under-secretariat of the Treasury will participate in certain decisions with financial implications.

Contractual Structure

The government will in each case enter into an implementation agreement with the relevant project company setting out the terms on which it will undertake each PPP project.

The private sector concession over a road PPP project may be up to 49 years. However, in practice it may be considerably shorter. For instance, the operation period of the third Bosphorus bridge, part of the Northern Marmara Highway Project and which was tendered in May 2012 to be constructed and operated under the BOT model, will be 10 years. Similarly, operating rights of the two Bosphorus bridges and eight motorways have been transferred to the private sector for a period of 25 years.

In both greenfield and brownfield projects, the project must be transferred back to the government at the end of the operating term, in good working condition, at nil cost and without any encumbrances.

The project company will be strictly liable for any damage caused by the road project. However, presumably it would cover this risk by passing it on to its subcontractors and insurance.

Turkish law governs the implementation agreements. The dispute resolution mechanism under the implementation agreement can be either arbitration (which can be international arbitration if there is a foreign element - foreign arbitration awards are recognized in Turkey as it is a signatory to the New York Convention) or the courts. As road PPP projects are governed by private (not administrative) law, the relevant courts are judicial and not administrative.

The project company may only assign its rights or transfer its obligations under the implementation agreement upon an affirmative opinion from the awarding authority (Ministry of Transportation, Maritime Affairs and Communication or Privatization Administration, as the case may be), and with the prior consent of the relevant minister.

Financial Terms

When tendering a road project, the government may ask for upfront or periodic payments, or a combination of the two. In addition, for brownfield road projects, the project company may be required to continue to offer services at regulated tariffs for specified periods. For both greenfield and brownfield projects, there could also be obligations to encourage cost separation in order to ensure fair and competitive pricing.

With respect to any state subsidy to be provided to the project company (and thereby built into its revenue structure), there are two options as to how the state may structure such a subsidy. These are a demand guarantee (meaning a guarantee that there will be at least a minimum traffic flow), and a guarantee of the debts owed to the road PPP project's lenders. For instance, it is understood that for the construction and operation of the third Bosphorus bridge, the government guaranteed a minimum traffic flow of 135,000 cars per day and provide certain minimum guarantees as to the tolls that traffic would generate.

If the project company fails to fulfil its obligations under the implementation agreement, the government has certain rights to step into the project, including taking over certain contractual arrangements that the project company has put in place. For example, in relation to greenfield projects, to explicitly confirm that the relevant part of the government has the right to assume the financing obligations of the project company, in the event that the implementation agreement is terminated prior to the expiry of the operating term.

There are exemptions from value added tax for road PPP projects. Furthermore, the actual deal documents are exempted from stamp duty and fees. Double taxation agreements and bilateral investment treaties to which Turkey is party provide certain additional limited protection to foreign sponsors and lenders.

When the implementation agreement is signed, the project company will need to provide a bid bond of 1% of the total investment required to undertake a greenfield road PPP project. The equity part of the financing that the project company obtains should be at least 20% of the expected fixed costs of the project.

Regulatory Issues

Various consents are required to undertake a road PPP project, such as planning permission and obtaining environmental clearances.

Obtaining planning permission includes having the relevant zoning plan amended (the zoning plan for an area includes details of any planned construction), and obtaining the consents required for certain types of land. Amending the zoning plan can be a challenge. Even if changes to the zoning plan are approved by the relevant municipality (and by the Ministry of Environment and Urbanization, as the case may be), the approval is open to challenges in the courts. For example, there were reportedly 1,514 objections raised to changing the Istanbul Metropolitan Municipality zoning plan for the Northern Marmara Highway Project, and litigation arising from this is ongoing. As a general rule, challenges to administrative actions and decisions (such as municipality approval) do not interfere with execution of the implementation agreement, as long as no stay of execution has been secured. No stay of execution has been issued for the third Bosphorus bridge project, and the project was tendered in May 2012.

Any new highway or road with more than four lanes requires an environmental impact assessment. An opinion will also be required from the Ministry of Environment and Urbanization that any negative environmental impact of the project is acceptable.

Such projects will be affected in other ways by the road PPP project regulatory framework. For instance, reflecting Turkey's history, the Ministry of Culture and Tourism has the right to direct that action may be taken by a project company to protect antiquities: this may include suspending work at a site while the antiquities are removed.

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Earlier articles in the series focussed on Turkey's Ports, Airports and Healthcare PPP markets.