



T.E.I. Thessaloniki
Greece



Department of Tourism
Management

UDC 347.471.031(497.5)
Preliminary communication
Received: 03.10.2006

STATE AND LEGAL FRAME FOR PUBLIC-PRIVATE SECTOR PARTNERSHIP IN REPUBLIC OF CROATIA

Jože Perić
Jasenka Štiglec
University of Rijeka, Croatia
State Inspectorate of the Republic of Croatia

Abstract: Public-Private Partnership as a model of financing the development projects claims for the active role of the state, especially regarding the legal frame and conditions. After the increasing importance of the partnership in the last twenty years and the individual encouragement, the EU plans the legal initiative on the level of the whole integration.

For the countries in transition and Croatia as the specific case, partnership can be one of the key generators of development acceleration. Within the assumptions for partnership, the legal frame is the necessary prerequisite of the partnership.

Key words: Public-Private Partnership, legal frame, Croatia.

Sažetak: DRŽAVA I PRAVNI OKVIR PARTNERSTVA JAVNOG I PRIVATNOG SEKTORA U REPUBLICI HRVATSKOJ. Partnerstvo javnog i privatnog sektora kao model financiranja razvojnih projekata zahtijeva aktivnu ulogu države, naročito u pogledu pravnog okvira i uvjeta. Nakon rastućeg značaja partnerstva zadnjih dvadesetak godina i pojedinačnih poticaja, Europska unija planira i pravnu inicijativu na razini cijele integracije.

Za zemlje u tranziciji, i Hrvatsku kao specifičan slučaj, partnerstvo može biti jedan od ključnih generatora razvoja. Na bazi partnerske kooperacije s domaćim i stranim privatnim izvorima financiranja Hrvatska može ostvariti značajan dio projekata značajnih za ubrzanje razvoja. Uz druge uvjete, primjeren pravni okvir je neophodan poticaj partnerstvu.

Ključne riječi: Partnerstvo javnog i privatnog sektora, pravi okvir, Hrvatska.

¹ **Jože Perić**, Ph.D., Full Professor, University of Rijeka, Faculty of Tourism and Hospitality Management in Opatija, Croatia, **Jasenka Štiglec**, M.Sc., grad. in law, State Inspectorate of the Republic of Croatia, Zagreb, Croatia.

1. INTRODUCTION

The beginning of public and private sector partnership spreads in long past. In recent time, especially since last century 80-tis, in addition to growing appliance of neo-liberal concept of economies and role of state, Public-Private Partnership has come through specific way, model of solving development needs and satisfaction of requirement for many products and services.

The practice of Partnership is most developed in developed countries, but also characterizes developing countries, especially in the field of infrastructure and in relationship with private investors from abroad.

For countries in the transition, and Croatia as specific case, partnership could be one of the key generators of growth.

In contexts of this paper it is emphasized that legal, and interdependently, legal-administrative frame for Private-Public Partnership has been one of the first precognitions for realization of sectors cooperation models. Intelligible, the significance of legal frame is larger as the country is less developed, respectively to correlation with desirable speed of commutation to developed countries.

Croatia has made first steps on affirmation of Partnership and recorded first concrete implementations. Nevertheless, that does not mean that precognitions should not be upgraded and improved.

2. STATE AND PUBLIC – PRIVATE PARTNERSHIP

Domination of neo-liberal concept of economy, especially in the European region, with reduction of state role and its institutional forms, has opened the room for contrivance of new models for achievement of effectiveness and development which should ensure the state quality and accessibility improvement of products and services without additional assignment of financial resources. As one of the solutions appeared the Public-Private partnership as a network representative of possible connection between interests and goals of state-public sector and private sector.

To enable the Public-Private Partnership it is essential the presence of given requirements in order to recognize them as real alternative of problem solution. Thereby should be emphasized that without state it is not possible to conduct Public-Private Partnership, because it represents the body that includes and introduces this system in the frame of its plans and judgments to achieve the system goals.

PPP project is not novelty, it has been for long and with success used by many European countries. It is specially developed in Great Britain, where since 1992.the government has inaugurated this model with the aim of private capital engagement in investments of public importance, improvement of conditions and total value of

constructed buildings, same as more rational usage of financial resources collected from rate payers.²

2.1. State interests

For the purpose of this paper only the state interests have been examined. In that context it is important to emphasize the way that state interests in Public-Private Partnership project are manifested in³:

- continuity of providing services through whole time period. The state does not wish to withhold services to its citizens (e.g. provision of electricity, water and natural gas), independently to deferent interests and possible problems with private sector;
- switching the risk to private sector. The state shows interest in allocating the project risks on private sector too in order to reduce the expenses. Private sector administers better with risks, especially the ones related to market;
- spreading of financial resources and increasing of financial possibilities. Private sector presents the available financial resource. Faster development and modernization have been obtained, which is especially important for some services as e.g. tourism;
- realization of development projects in short time period and distribution of costs in longer period;
- interest of public sector which is connected with constant environmental protection, human health care, insurance, quality and standards of services. The state strive to accomplish it through projects which apply the method of Public-Private Partnership;
- achieving the larger value for money and better services for the same price;
- development of local market, local banks and commercial multilateral foreign direct investments;
- etc.

The state can accomplish its own interests through active partnership through leaning on private sector and nongovernmental organizations, to share with them the responsibility and to collaborate with them on accomplishment of basic state goals:⁴

- dynamic economy based on knowledge and educated individual,
- state does not command but encourage, market serves as power force in private and public interest,
- promotion of civil society,
- modern state government should be based on collaboration and decentralization.

² Construction Industry Council (1988): *Constructions' Key Guide to PFI*, Construction Industry Council London

³ Bajrambašić, I.M., *Achievements in finance of infrastructure: Public and Private Partnership*, Private Finance Initiative, Sarajevo, 2004., pg. 67

⁴ Perić, J., *Public Private Partnership, Fintrade & tours d.o.o.*, Rijeka, 2006., pg. 34 (in press)

2.2. The role of state in Public-Private Partnership

The role of state is very important and it is impossible to conduct the Public-Private Partnership without the state. Notably, the state defines the ways of private financial initiative implementation and Public-Private Partnership. It identifies sectors, as well as projects which are necessary to realize. Through its regulations the state encourages and prepares the framework for implementation and application of Public-Private Partnership system.

To understand the role of state in Public-Private Partnership it is needed to understand the changes in disposition of present state in the context of its capabilities. That change has been achieved in two main directions, from interventionist to proactive market role on the field of market functioning, and from centralistic role to greater activation of entrepreneurial sector on social field. The capability of state should be connected to its power of market ineffectiveness, and inequality and lack of emancipation in the society removal.

Thereby it is possible to distinguish three levels of state capability:⁵

- minimal level of care for provision of basic public goods (defense, law of legal order, protection of proprietary rights, macroeconomic stability of public society system)
- intermediate level implies basic care for environment, basic education of people, regulation of market structure and monopole, financial regulation on capital market and in public finances, protection of customers rights, social security and help for unemployed
- the third level is connected with proactive coordination of private activities, strategic encouragement of competition in open market, privatization and deregulation of public and social funds.

The traditional responsibility of state for public goods is the one that is connected with minimal level of care for supply of basic public goods.

On the second level the state still has significant role, but shares it with other bearers of services as are commercially focused state agencies, entrepreneurial subjects and civil society.

Only on third level the question of creation of alternative approaches to solutions of contemporary development problem becomes valid so here one could search for the source of Public-Private Partnership creation. The growth of state ability on third level require radical reform of social state and its institutions, first of all better management and more effective leading of public administration and market directionality to production, distribution and consumption of public goods.

Government agencies (state) are very active in implementation of this system because the projects would not be achievable and sustainable without their work.

⁵ Kovač, B., „Nekakeri vidiki politično ekonomske analize sodobne loge države in trga v Sloveniji“, Teoreija in praksa, No.3, 2000, pg. 515

Absence of state in some cyclically defined segments, as financing and alike does not mean that state does not participate in project.

From the state viewpoint is important for the partnership to recognize, that is to notify the need of determination according to following features:

- development policy of state, including introduction of Public-Private Partnership as important segment of development
- promotion method and intensity of Public-Private Partnership
- legal frame
- commercial frame
- sectors and subjects submissive to application of Public-Private Partnership
- development projects
- forms and methods of state support for Partnership system, including risks, financing, facilities and alike.

Because of so important state role the entirely arranged legal (and interdependent commercial) frame for Public-Private Partnership implementation is needed.

3. LEGAL FRAME FOR PUBLIC-PRIVATE PARTNERSHIP

Many, especially European countries, in significant extent have adapted their regulations (legislation) to possible application of Public-Private Partnership. However, during time, parallel with growing of awareness about potential partnership, more and more intensively the need for legal regulation of this collaboration models has been indicated on the level of European Union as whole.⁶

Term of Public-Private partnership has not been unambiguously defined on EU⁷ level, but European Commission documents exist that are used as instructions for application of those models.⁸ Public-Private Partnership refers to different forms of collaboration between bodies of public sector and private entrepreneurship, whose goal is to provide financing, construction, reconstruction, management or maintenance of buildings or provision of services. Clear financing of public projects form private sources is not regarded as PPP. PPP satisfies the need of private financing of public projects and provides greater value in public life that Know-how and working methods of private sector offer. The main characteristics of PPP in relation with public sector is that PPP defines outputs and not inputs, transfers risks on private sector, the budget is not burden, the financing is more efficient in comparison with traditional model and the safety of future costs and quality is greater. In relation to private sector the main

⁶ For example one could quote Danua Hubner, in charge of Regional Policy Of EU „The public sector alone does not possess the capacity for realization of needed infrastructural projects of large scope ... to be brutally open, we do not think that we could without involving of private capital“and further, Charly McCreevey, in charge of internal market has stated: ”Clearly that the private initiative is needed on the level of EU”, Competitiveness Digest No. 10, more on <http://www.euroactiv.com/en/innovation/public-private-partnerships-key-cohesiongrowth/article -158748>

⁷ In english, JPP is known as PPP (Public-private Partnership)

⁸ See: Green Paper, European Commission, COM (2004) 327, Guidelines for Successful Public-Private Partnership (March 2003.)

characteristics of PPP are: ensures financing, fastens the project implementation – conceives, constructs and manages, it is paid for services after delivery, pays penalties if the deadline and/or quality has not been respected and returns the property to public sector after the contract finishes.

3.1. The experience and determinants of legal frame

The overall development economical and social policy is based on incentive legal frame that enable safety and business attractiveness for partners – investors. Profit achievement in honest and truly competition with safe legal frame represents the attractive element for investors that continuously search for new business possibilities.

That could be especially applied if the country desires for direct foreign investments (FDI – foreign direct investments) that could be acquired through models of Public-Private Partnership because these models are diverse and adaptive to circumstances and distinctiveness of state. This interest exists particularly in transit countries, developing countries and undeveloped countries. To enable the attractive projects and investment guarantee the state also practice legal changes that would provide the achievement of desired conditions.

In order to conduct the PPP projects, many European countries have established specific regulations or guidance that serve as legal frame or that are used to beam and encourage conduction of these kinds of projects. European Commission highlights that these could not serve as a solution for all problems and that all projects, even the ones realized with juncture of public capital and private investments require the estimation if the investment would lead to benefit for the community and would its input be more significant from outcome made by “more traditional kind of contract”. According to *acquis*, PPP represents perfectly clean arrangement and does not require adoption of new legislative. Decision with whom and how would assemble contracts lies on public government, and the basic elements of European Commission view on PPP question are found in her Green Paper about PPP and European laws of contract and concessions.⁹ Namely, every legal act, contractual or unliterary, by which the public body accredits the praxis of economical service to third person, must be harmonized with regulations and principles that are concerned with freedom of services providing and commercial origination (article 43. and 49. Contract about EU), and that particularly embraces the principles of transparency, equal treatment, throttling and mutual recognition.

The Greece could be quoted as example for the reason that has customized its legal regulations to this model and started construction of many objects in different areas of infrastructure: railroads, subways, tunnels under water, telecommunications, harbors, highways, network of fuel distributions, etc. Beside Greece and the other EU countries (England, France, Ireland, Island, Germany, etc.), including the ones that are not members, have changed its regulations in order to use the system of partnership of

⁹ Privredni vjesnik – Prvi hrvatski poslovno-financijski tjednik, br. 8. „Europski poučak“, Javno-privatno partnerstvo u Europskoj uniji, Brže i više za iste pare

public and private sector for development projects. In that way, many projects have been initiated based on principles of Public-Private Partnership.

These legal modifications represent in one hand alleviation of regulations that could create some risks for state ("state risk"). On the other way this increases concern of investors for direct investments (FDI) in country because state provides the warranty for investment, profit growth possibility, etc.

Legal frame cannot be defined as uniquely usable to all countries, because its numerous conditions and coverage significantly differ from country to country. Change of legal frame shouldn't be quick and radical. Accordingly, rules shouldn't be rigorous and should be harmonised with the context of functionality. Planning the introduction of new legal frame represents the most appropriate way of changing regulations because it is not causing violation of existing regulations, which has a serious impact on economy and society.

In that context, it's needed to be defined:

- which regulations should be changed
- which new specific regulations should be adopted
- which are deadlines for introducing the regulations
- which elements are defined by regulations and which by partners of public private partnership.

Public institution's role and function should be determined by regulations. Some elements should be defined completely, in order not to interfere with the system of public private sector; whilst some elements should be defined through negotiations on project's and sector's conditions. Regulations should precise and define responsibility and procedure in the process of choosing a partner, negotiations etc. Identification of this area in general, ensures transparency and public control, which is a significant element of successful public private partnership.

In wider consideration, legal frame imply clearly defined business and entrepreneurial frame in a state which is introducing and accepting methodology of public private partnership for development and financing. Such approach facilitates private enterprises and investors to bring decision on financing and realisation of project.

It is obviously that private sector is not willing to invest in projects which aren't offering clear and favourable conditions. Therefore, the analysis of market and prices is inevitable because the investors decide on basis of return on investment and profit.

Business frame is linked tightly to legal frame. Private sector asks for clearly defined elements of these two frames in order to have safe and legal state's guarantees for investment, risk and profit expected. Regulations that define business frame should be in accordance with state's business strategy objectives of public private partnership. Strategy of development of specific sector and national economy is important to potential private investors to assess overall situation, plans, measures, specific economical categories such as the price policy, interest rates, inflation rate, other significant projects etc.

Private sector requires the more information and data on costs, revenues and risks to assess the project.

Beside the information, all potential investors ask clearly defined legal regulations that provide protection of private enterprise's intellectual property, integrity and market freedom.

By definition business frame represents vast range of measures and regulations. However, some elements are compulsory and should be defined in advance. Those are¹⁰:

- Law on protection of intellectual property rights (licence, equipment, land, and other rights)
- Law on protection against nationalisation of equipment and other ownership
- Possibility of fulfilling the contract is a significant element, which ensures safety in fulfilment of complex public private partnership contracts
- Financial, bank and assurance regulations
- Labour law
- Environment law
- etc.

Approaches to business frame are different and depend on type of project, sector, economical and social conditions.

In order to understand better business frame regulations, these are divided into following groups¹¹:

- a) economic regulations that refer to:
 - prices
 - level of services
 - competition policy
- b) non-economic regulation that refer to:
 - quality
 - environmental quality
- c) social regulations that refer to:
 - social rights
 - employment
 - business flows and customs etc.

All these regulations are important for business frame and their significance vary depending on purpose and objective of a project.

Abovementioned regulations are possible and depend directly on participants of the project behalf and on project's attractiveness for private financing. It's important

¹⁰ Perić, J., Dragičević, D.: «Public private partnership in tourism – global experience», 18th international congress Tourism and hospitality 2006.: New trends in tourism and hospitality management, 3-5 June 2006, Opatija

¹¹ Perić, J., op. cit., p 58

that state carries out detailed analyses and estimation of revenues, costs and other elements of the project which are crucial for project realisation. State has to be realistic in its estimation. Also, state should be aware of market conditions to use supporting measures and to achieve best project contract and realisation.

3.2. Public private partnership legal frame

Legal frame of public private partnership can vary significantly, depending on different terminology. According to European Union Green book there are several types of PPP's that are based on contract exclusively and institutional types. There are several types of exclusively based on contract PPPs that differ regarding four main elements of partnership: building, management, financing and ownership.

Main types are:

- **Private financial initiative (PFI).** This type of PPP is most common in Great Britain and also, in many variations around the world. A private enterprise designs, finances, builds, maintains and manages the building built for public sector (for example school, hospital, communal infrastructure). Public partner, on regular basis, not user, gives a fee to private partner for usage of the building or service. A fee could be fixed or arranged accordingly to availability of building or service.
- **Concession.** Public sector assigns to private firm, that is investing its own capital, the right to exploit specific services, for which public sector receives compensation. Particularity of this type of PPP is direct connection between private partner and final user. Private partner provides direct service to final user instead of public partner, but under its control. Concessionaire receives a fee that consists of customers' usage fee or sometimes state's support tariff.
- **Lease.** The private partner doesn't invest its own capital, but manages and maintains the system and invoices end users directly.
- **Build Operate Transfer (BOT).** The private partner builds, owns and manages the infrastructure for a certain period, after which transfers the infrastructure to public partner.
- **Build Own Operate Transfer (BOOT).** The private partner has a franchise to finance, design, build and manage the infrastructure and also, to invoice end users during the certain period, after which the ownership is transferred to public sector.
- **Buy Build Operate (BBO).** The settlement of the transfer of public infrastructure to a private partner is arranged in a contract, by which the private partner will improve and manage the infrastructure for a certain period.
- **Build Own Operate (BOO).** The private partner builds and manages the infrastructure but retains ownership.

3.3. Private public partnership legal frame in Croatia

To facilitate the process of electing and contracting the building infrastructure within private public partnerships, the government of Republic of Croatia on the 1st of September 2006 brought The Conclusion on Guidelines for private public partnership contracting forms.¹² Subparagraph 3, "The types of private public partnerships", provides that these guidelines refer exclusively to contractual types of PPPs. According to these guidelines public partner can be: the Republic of Croatia through authorised ministry, public institution and company that is in majority owned by the Republic of Croatia, local or regional self-government (county, city and municipality), public institution and company that are in majority owned by local or regional self-government. The public partner can participate in a project with things or rights (donation, lease of a land, concession, building permit, transfer ownership of building or project documentation that the private partner accepts and respects regulations on rights and commitments), but mostly, private partner participates in projects through payments for private partner's services. Moreover, guidelines provide types of long term contracts between public sector and private partners that are not considered as private public partnership: long term contract on services, by which the public sector acquires only services, e. g. maintaining without capital investments; contract on design and build of infrastructure for public sector; establishment of new company that is jointly owned by public and private partner; establishment of joint venture; state guarantees; financial leasing contracts, in which public sector uses infrastructure owned by private company and pays a fee during certain period of time; partly or complete privatisation of state's assets by private operators.

Main characteristics of PPP - BOT and PFI projects in Republic of Croatia are as follows:

- Public and private sector (building performer, consultants, financier etc.) operate jointly on "specific" project through especially formed company, so called Special Purpose Company.
- All project stages are involved (design, build, financing, maintaining and utilization of building) during the "economic lifetime" of a building (25 – 30 years).
- Private sector bears main risks.

Public building's capital costs are not included into current duties of a public sector (according to EUROSTAT guidelines), and also, taxpayers do not pay cost of repairs and deficiencies occurred during the utilization of a building, which represent significant advantages of PPP types mentioned.

Fostering the usage of PPP's, Government of Republic of Croatia actively stimulates informing on PPP by conducting continuous educations and professional seminars (more than 30 seminars and workshops for public sector representatives have been organised) and also stimulates informing on legislative (Law on Private public partnership, Law on public procurement and Law on concessions). Nevertheless, during the negotiations on joining to EU, Croatian representatives actively work on

¹² The conclusion on guidelines for private public partnership is published in "Narodne novine", no. 98/06.

adjusting Croatian legislative. In Republic of Croatia there are no legal barriers to realisation of PPP's; until new regulations are being adopted current legislative provides regulations on the "build right" (Law on ownership and other rights), "availability risk" and concessions (Law on concessions).

First Croatian PPP projects are successfully realised using the PFI type in building public buildings: schools and sports halls in Varazdin County and in Koprivnica (25 year contracts). Concession types are common in building the infrastructural projects: aquatron in Zagreb (25 year concession) and Zagreb – Macelj highway (part of Trans European highway 10A, 25 year concession).

There is an increasing number of supporters of PPP in tourism industry aiming to faster building and managing of tourism and hospitality infrastructure, which could positively effect on raise of quality in a tourist destination, extend of tourism activity to whole year, increment of number of tourists and opening of new jobs. Altogether it could contribute to growth of life standard and animate secondary economic activities directly or indirectly related to tourism and hospitality. Realisation of tourist projects by model of PPP with private capital, innovations and know-how could accelerate Croatian tourism animating attractive and poorly exploited tourist destinations.

Potential restriction in public sector in applying PPP, represent difficulty in estimation of total costs during the lifetime of a building and length of period for consign of building. Time needed for preparation of PPP project lasts, in the most of EU countries, 12-24 months (since start of preparation till signing the contract and start of building). Implementation of PPP project brings higher quality, more efficient public service, known total cost of ownership public buildings (including maintaining and utilisation), committed services paid only, long term savings of total life costs (savings on a level of 17% current value are proven in EU countries).

In circumstances of preparation for EU membership, PPP contributes to further market and state's portfolio stability, which directly influences on maintaining trend of increasing direct foreign investments.

4. CONCLUSION

Like many other countries, beside development of market society and neoliberalism concept of economy, Croatia accepted development of various types of partnerships between private and public sector.

Prescribed political and legislative basis for development of partnership and successfully realised first projects, Croatia is making effort to regulate legal and business frame in order to enable cooperation between the sector within the country and among relations with various foreign finance sources.

Current legal frame provides stimulating starting point for development of partnership in Croatia. However, it is necessary to constantly improve legal frame in order to make partnership one the main starters of development.

REFERENCES

- Kirkpatrick, C, Parker, D., Zhang, Y. (December 2004): "Foreign direct investment in infrastructure in developing countries: Does regulation make a difference?", Centre on Regulation and Competition, University of Manchester and Cranfield University
- Mistry, P. S., Olesen, N. E. (September 2002): "Foreign Direct Investment in LDCs: The Role of Public Private Interaction in Mitigating Risks" - Executive Summary, September, 2002
- Public Private Partnerships (2006), Effective competition, vital to extend reach and use of ICT, World Bank, 10 March
- Construction Industry Council (1988): Constructions' Key Guide to PFI, Construction Industry Council, London
- Bajrambašić, I.M. (2004), Achievements in finance of infrastructure: Public and Private Partnership, Private Finance Initiative, Sarajevo
- Perić, J. (2006), Partnerstvo javnog i privatnog sektora, Fintrade & tours d.o.o., Rijeka
- Kovač, B. (2000), "Nekateri vidiki politično ekonomske analize sodobne loge države in trga v Sloveniji", Teorija in praksa, vol. 37, br. 3, str. 509-525
- Competitiveness Digest, No. 10, <http://www.euractiv.com/en/innovation/public-private-partnerships-key-cohesion-growth/article-158748>
- Green Paper, European Commission (ožujak 2003), COM (2004) 327, Guidelines for Successful Public-Private Partnership
- Perić, J., Dragičević, D. (2006): "Partnerstvo javnog i privatnog sektora u turizmu - svjetsko iskustvo", 18. bienalni međunarodni kongres Turizam i hotelska industrija 2006.: Novi trendovi u turističkom i hotelskom menadžmentu
- "Narodne novine" broj: 98/06.

Copyright of *Tourism & Hospitality Management* is the property of *Tourism & Hospitality Management* and its content may not be copied or emailed to multiple sites or posted to a listserv without the copyright holder's express written permission. However, users may print, download, or email articles for individual use.