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An overview of this issue

I am delighted to introduce this fifth issue of **Infra**Read, our biannual publication in which we cover a range of legal and transactional issues relevant to the transport and infrastructure sectors from our offices across the globe. In this issue, we look at:

AUSTRALIAN INFRASTRUCTURE (p3) In September 2013, the Australian Prime Minister, Tony Abbott, declared *"I want to be known as an infrastructure prime minister"*. Murray Wheater provides an on-the-ground overview of the current Australian infrastructure market, including detailing the major opportunities which are opening up as well as discussing the key legal issues which foreign investors in Australian infrastructure need to be aware of.

INFRASTRUCTURE OPPORTUNITIES IN KSA (p8) The Kingdom of Saudi Arabia (KSA) is injecting large sums of money into modernising and expanding its transport infrastructure network. Joss Dare and Faisal Baassiri investigate how investment in transport infrastructure is now one of the main factors driving KSA's growth after the slowdown of the construction industry in 2012.

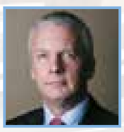
UK NHS (p13) The UK's NHS, like any other public service, is subject to the will and whim of its public paymaster, whose objective will be to preserve a well-loved institution while, at the same time, cutting costs. Jane Staveley investigates how both "keeping and cutting" may present some interesting new opportunities for the private sector and ease the pressures on the NHS.

TAX (p16) In September 2014, the Organisation for Economic Co-operation and Development, as part of its ongoing action to combat Base Erosion and Profit Shifting (BEPS), issued its report on Action Plan 6 entitled "Preventing the Granting of Treaty Benefits in Inappropriate Circumstances". Nicholas Gardner considers the potential implications of the report and the impact it will have on international infrastructure investment funds.

SPANISH AIRPORT PRIVATISATION (p19) The Aeropuertos Españoles y Navegación Aérea (Spanish Airports and Aerial Navigation) (AENA) privatisation represents one of the most ambitious projects undertaken by the Spanish Government in recent years. Over the past number of years, AENA has been implementing a viability plan, including the refinancing of its €14bn debt, to make itself more attractive to potential private investors. Gonzalo Jiménez-Blanco and José María Anarte discuss the implications of these impending changes.

G20 AND EU INFRASTRUCTURE INITIATIVES (p22) Increasing investment in infrastructure is high on the agenda of global leaders, with the Organisation for Economic Co-operation and Development estimating recently that some US$70tn in investment is required globally by 2030. Catherine Clarke provides a commentary on the G20's new Global Infrastructure Initiative and the EC's new Investment Plan for Europe, as well as giving an overview of the World Bank's and the United Nation's plans in this area.

I hope that you find **Infra**Read useful and enjoy reading this issue. Please let me know if you have any feedback or if there are any topics that you would like us to cover in future editions.



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AUSTRALIAN INFRASTRUCTURE

A guide for investors

by Murray Wheater

In recent years, there has been a renewed focus by federal, state and territory governments on developing infrastructure across Australia. This growing demand is driven by a number of factors, including: (i) Australia has an existing infrastructure deficit estimated at AU$770bn; (ii) Australia is facing sustained population growth driven partly by immigration, particularly in the major cities; and (iii) there has been rapid growth in freight and passenger transport demand and this is expected to continue.

Investment in Australian infrastructure is supported by a favourable (although complex) regulatory environment. It is a relatively mature market, which had its beginnings in the privatisation wave of the 1990s. This contributes to a lower level of risk, obviously an important factor for overseas investors desiring stable cash flows.

Types of assets

Social infrastructure PPPs

Australia has one of the most advanced social infrastructure Public Private Partnership (PPP) regimes in the world, making it an attractive opportunity for foreign companies.[1] Social infrastructure PPPs have been used in Australia to develop facilities such as hospitals, prisons and schools. Generally, investors do not bear any demand risk and returns to the private developer are through availability payments.

Rail

There are a number of forthcoming opportunities in the Australian rail market, driven by two factors:

- the need for the mining sector to find routes from "pit to port" for new and developing mines; and
- plans for the construction of new passenger railway infrastructure, acquisition of new rolling stock and the restructuring of existing passenger networks driven largely by patronage growth, increased urbanisation and the need to modernise the network.

Overall, the priority of the federal government appears to be developing freight rail before funding the development of urban rail projects:

- **Western Australia**: this state has a number of independent railway networks which serve major population, industry, agricultural and mining centres. The Pilbara region in the north-west is dominated by substantial iron ore mines which require heavy haul

1 Business Monitor International, *Australia Infrastructure Report*, 2012.

railway networks to transport iron ore to port for export.

The rail industry has become highly regulated, particularly in the area of third party access. Western Australia has been driven to try and ensure rail infrastructure is not wholly controlled by the track owners at the expense of rail operators and their customers.

- **Queensland**: the coal freight network is operated privately by Aurizon, while the passenger networks and the remainder of the freight network are owned by state-owned Queensland Rail. In 2014, the Queensland Government finalised the "New Generation Rolling Stock" project, a AU$4.4bn PPP for the provision of 75 new six-car trains with a 30-year ongoing maintenance contract.

  It is expected that Queensland Rail will restructure to franchise the network to take advantage of private sector innovation. Queensland also presents significant opportunities in "pit to port" mining infrastructure.
- **New South Wales**: much of the rail infrastructure in New South Wales is owned and operated by entities owned by the state government. The main opportunities and changes are likely to be around passenger railways rather than mining railways. Two of the largest PPPs in New South Wales are the North West Rail PPP and the Sydney Light Rail PPP, which were both finalised in 2014.
- **Victoria**: Victoria has seen the most private sector involvement in the operation, maintenance and development of the passenger rail network. For instance, the train network is currently operated by a consortium led by Hong Kong's MTR Corporation. New projects for passenger rail lines have recently been announced.

The conclusions which can be drawn are that:

- there are major investment opportunities both in passenger and freight railways;
- in many of the rail sectors, there is a relatively thin market when compared with overseas markets; and
- while the projects are politically, commercially, technically and legally complex, given the desire by all governments for implementation, many of them will be delivered.

Roads

Although the past decade has seen significant investment in the Australian road system, population forecasts and the rising number of cars per household indicate that significant new investment in roads will be needed in the coming years, particularly in high urban growth areas.

Historically, governments have been reluctant to strain their balance sheets with the high levels of debt required to fund significant road assets, and have therefore made use of private financing. In Australia, sourcing revenue through user-pay tolls has been a common funding model, with the private sector taking patronage risk based on traffic forecasts.

However, this funding model, as applied in a number of high-profile projects (such as the Lane Cove Tunnel and the Cross City Tunnel in Sydney, and Airport Link and the Clem Jones Tunnel in Brisbane), has led to financial difficulty for the private operator as a result of the actual road traffic being significantly below forecast levels, on account of an over-allocation of traffic revenue risk to the private developer. Against this backdrop, governments are recognising the need for alternative funding models to be considered, including:

- government contributions;
- shadow tolling (where a toll is paid by the Government);
- payment by government of ongoing availability payments (as used by the Victorian Government in the Peninsula Link road PPP); and
- funding the initial stage of the investment and seeking private sector involvement after traffic usage levels are established (as is being considered by the New South Wales Government in the proposed WestConnex motorway PPPs).

The main types of roads-related transactions include:

- PPP road concessions;
- operation, maintenance and expansion of existing toll roads (including refinancing opportunities);
- large-scale upgrades of non-PPP roads (such as the Pacific Highway upgrade); and
- electronic tolling and associated infrastructure issues.

Ports

Port-related infrastructure projects currently present attractive opportunities to international infrastructure investors. Reflecting the importance of ports in the Australian economy, activity in this sector has been buoyant in recent years. The main types of port-related transactions include:

- privatisations of government interests in ports;
- expansions of existing ports (including new terminals); and
- private-to-private sales of interests in existing ports.

The demand for new infrastructure, coupled with a perceived need by state governments to maintain or regain high credit ratings, has placed pressure on governments to privatise some ports in order to fund vital new projects. Recent port sales in Brisbane, Newcastle and Sydney have been met enthusiastically by the market, with state governments generating serious interest from offshore investors looking to diversify by investing in the Australian economy. Victoria, Western Australia and Queensland have announced plans to privatise other port assets, although these ports predominantly service bulk commodity producers.

Resources-driven activity in Australia is helping to fuel a number of port development projects and there are a number of projects at the planning stage for both bulk commodity and container terminal expansions.

In addition to resources-driven port development, growth in freight to, from, and within Australia's capital cities is placing increased pressure on existing container handling facilities, forcing a number of state governments to look at new projects. By 2030, the number of container movements through Australia's ports is expected to be two and a half times that of 2007.[2]

Airports

Australia's network of airports forms an integral part of the national economic infrastructure. They are largely monopolistic businesses. The Australian Government has identified investment in airports as a key objective. Meeting demand will require significant investment, particularly to upgrade local gateway airports. Almost AU$9bn worth of necessary upgrades and improvements is in the pipeline over the next decade to cope with the predicted increase in airport traffic.[3] In particular, planning has accelerated for a second airport for Sydney at Badgerys Creek to the west of the city.

Between 1997 and 2002, 22 of Australia's major airports were privatised under 99-year lease arrangements with the federal government. These leases have given control of all airport developments to the private operator and are regulated under the Airport Act 1996.

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2 *Nation Building: Driving Australia's Productivity* (May 2012).

3 *Australian Aviation*, January/February 2013.

Water
Involvement in the water sector has been more limited than in other sectors. Despite this, several state governments have procured desalination plants to remove salt from sea water in order to supplement traditional water supply systems for large urban areas. Desalination plants have been built in Queensland, New South Wales, Victoria, South Australia and Western Australia, with foreign companies involved in these projects.

Private infrastructure for the resources industry
Supporting infrastructure is a critical component of any resource venture. Given the remote locations of some resource projects, this infrastructure is often provided as part of an integrated self-contained development. Any subsequent transfer of the interests in these projects would include the associated infrastructure. Where infrastructure is developed by a particular resource project, there are legal obligations to allow access to neighbouring resource projects (see "Access regimes" below).

In less remote locations (e.g. Queensland), government-owned and privately owned roads, railways and ports support the resources industry. However, the existing infrastructure is inadequate to accommodate future growth.

Project pipeline

Although it is now more than a year since the Liberal/National Coalition Government was elected, there is still some uncertainty as to how it will prioritise different infrastructure needs. The Government has announced some of its infrastructure priorities and construction timetables and these will be developed in conjunction with state and territory governments. The federal government has also announced an AU$5bn asset recycling initiative to incentivise state governments to sell assets and invest proceeds in new infrastructure.

PPP Model

According to Business Monitor International, "*a key factor underpinning [Australia's] attractive operating market is the strong platform it provides for Public Private Partnerships (PPP). Australia has one of the world's most mature PPP markets and, over the past two decades, has pioneered the delivery of complex PPP projects, developing a model that other countries, notably Canada, have sought to emulate*".[4]

Continuing commitment to the delivery of infrastructure through PPPs is evidenced by work at both the federal level and the state and territory level to streamline the PPP pipeline, and to refine the PPP model so as to maximise its application in a changing economic landscape. Today, the Government's appetite for PPP remains strong, despite a difficult period in 2008–10 as a result of the global financial crisis. Infrastructure is still a fundamentally attractive asset class from the perspective of the private sector, as it provides a secure investment through a long-term contract with government and, often, a government-backed revenue scheme.

The PPP model has been used to successfully deliver infrastructure across a very broad range of sectors. While the market is currently dominated by large transport (particularly urban road and rail) projects, rolling stock solutions, custodial facilities, schools, hospitals, car parks, court facilities, defence and educational accommodation, convention centres, sports stadiums, social housing, desalination plants and other economic infrastructure have all been delivered on a PPP basis in Australia.

The challenges for Australian PPP

Australia has very large and diverse infrastructure needs but a relatively small pool of contractors able to undertake projects on a PPP basis. This has led to an increased need to attract new contractors into the market, in order to add to market capacity and also to ensure that Australia benefits from global best practice in this area.

4 Business Monitor International, *Australia Infrastructure Report*, February 2012.

New participants face various challenges in entering the Australian PPP market, including:

- perceived lack of certainty over project pipeline;
- a costly bidding process; and
- complex tax-driven investment structures.

Australian governments have been working hard to alleviate these issues in order to attract further players into the market (for example, it has recently become more common for governments to agree to reimburse some bid costs to losing bidders, and governments are conscious of the need to reduce bid timetables and to work with smaller lists of competing bidders).

Australia's infrastructure needs often involve projects with a very large capital cost. The trend is towards an increasing number of "mega projects", such as urban tunnel construction, resulting in projects with capital values in excess of AU$5bn. This, coupled with probity and process rules which often mitigate against funding sources being available to multiple bidders for PPP projects, creates financing capacity issues which need to be carefully managed by reference to the timing of bringing PPP projects to market.

An emerging feature of PPPs in Australia is for governments to contribute to the financing of the project. This is most prevalent where the capital costs involved are very high, where there are concerns about financing capacity issues, or when it is considered that government contributions will result in a better value-for-money outcome.

A series of high-profile PPP project failures (particularly in the toll road sector) have made it very difficult to finance projects featuring patronage risk. The market is currently dominated by PPP projects backed by stable government cash flows.

In the aftermath of the global financial crisis, debt financing in Australia is only available for relatively short tenors leading to heightened refinancing risks. The Australian governments are responding to this by drawing on international lessons to introduce structures designed to alleviate this risk.

PPP Guidelines – national framework

Since November 2008, all state and territory government agencies have been influenced by the National Private Partnerships Policy and Guidelines (January 2010) published by Infrastructure Australia (the National PPP Guidelines). The National PPP Guidelines are the agreed policy framework for PPP procurement and apply to most federal, state and territory government departments and agencies. They apply to projects where there is private sector investment or financing and where the private sector is involved in providing public infrastructure (including economic and social infrastructure) or non-core services.

The key objectives of the National PPP Guidelines include: value for money; ensuring projects are delivered in the public interest; optimal risk allocation; output performance specifications and probity; and transparency and accountability of governments. However, the guidelines acknowledge that individual projects will need to address project-specific issues on certain mechanical and risk allocation matters and that individual states may, in some circumstances, wish to approach commercial matters associated with PPPs in different ways. Consequently, the National PPP Guidelines need to be considered in conjunction with policies adopted by individual state governments.

- **Victoria**: procurement of public infrastructure in Victoria is subject to the policies of Partnerships Victoria, the state body set up to facilitate the procurement of infrastructure in Victoria. The Victorian Government released comprehensive guidance material entitled "Partnerships Victoria Requirements" in May 2013 which, together with the National PPP Guidelines, will apply to the next phase of Victoria PPP projects.
- **New South Wales**: in New South Wales, the procurement of infrastructure and associated services through PPP by any NSW government agency, including state-owned corporations, needs to comply with the National PPP Guidelines and NSW specific requirements, as set out in the "NSW Public Private Partnerships Guidelines", published in 2012. NSW

has recently established a state body, Infrastructure NSW, to facilitate the procurement of infrastructure and to develop a cohesive long-term strategy for infrastructure in NSW.

- **Queensland**: in July 2002, Queensland Treasury and Trade established a body, Projects Queensland, to enhance the Queensland Government's infrastructure delivery capability. Projects Queensland is responsible for the implementation of the Queensland Government's "Public Private Partnership Policy" (July 2011), which sets out the overall principles governing the Queensland Government's approach to PPPs in conjunction with the National PPP Guidelines.
- **Other states and territories**: South Australia, Western Australia and the Northern Territory have each adopted the National PPP Guidelines as their primary PPP policy framework, with various jurisdictional departures. In Tasmania, all PPPs are still run primarily through the Shareholder Policy and Markets Branch of the Department of Treasury and Finance.

Further legal issues to consider

Tax

Infrastructure investment in Australia is affected to a large degree by considerations of Australian tax law. In fact, for some PPPs, generating a tax-efficient outcome is the main driver of the corporate structure of the investment vehicle. Given the complexity of Australian tax law, issues relating to tax and stamp duty throughout the life of the project need to be carefully considered before commencing the project or investment.

Particular issues for investors to note include:

(a) **Investment and development stages**: landholder duty (a form of stamp duty) applies to the transfer of "fixtures" to the land which generally include all infrastructure assets, although exemptions may apply depending on the particular rules of the state or territory in which the asset is situated.

Normally, payments from a "debt interest" under Australian income tax law are deductible against Australian income and are subject to a lower withholding tax rate than an "equity interest". However, the thin capitalisation rules limit the tax deductions which may be claimed by non-resident investors – this is important as projects may be highly geared in this initial stage.

There may be a need to separate structurally the ownership from the operation of infrastructure assets to retain the "pass-through" benefit of certain trusts (i.e. where the beneficiary of the trust is taxed, rather than the trustee).

(b) **Operation**: withholding taxes apply to certain types of income generated by Australian tax non-residents, including a five per cent withholding tax for construction or activities related to construction. The withholding tax rates may be reduced through the application of double taxation treaties.

Where an infrastructure project is part of an energy or resources project, investors should also consider the application of petroleum resource rent tax and royalties imposed by state and territory governments on the extraction of minerals.

(c) **Disposal**: any gain by a non-resident when disposing of an investment is subject to capital gains tax in Australia if the investment is "Taxable Australian Property", determined in accordance with the relevant tax legislation.

Access regimes

In Australia, many publicly and privately owned infrastructure facilities are subject to access regulation. There are both Commonwealth and state statutory access regimes, as well as frameworks for infrastructure owners to submit voluntary access undertakings. Access regulation is particularly common for railways and ports.

Access regulation can have very significant consequences. A company investing in affected infrastructure should consider the potential for third parties to utilise an access regime to gain access to the infrastructure. Providing access to third parties under an access regime may significantly affect the commercial returns to a facility owner, as well as limiting the owner's operational control and flexibility in its use of the infrastructure. Third party access may also impose regulatory and compliance costs, including involvement in expensive disputes.

Conversely, an investor interested in using another company's infrastructure facility may have the option of negotiating access under an existing access regime, or applying to have the infrastructure facility subjected to an access regime.

Part IIIA of the Competition and Consumer Act 2010 (CCA) establishes a national regime for access regulation which can be applied to nationally significant infrastructure.

Under the CCA, an infrastructure owner may seek approval from the Australian Competition and Consumer Commission for an access undertaking which is offered on a voluntary basis by the infrastructure owner. This access undertaking is intended to provide a framework for negotiation of the terms and conditions upon which the owner will provide access to third parties.

Other legal issues

There are a number of other legal issues of which participants in the infrastructure sector should be particularly aware, including the foreign investment approval regime, labour relations, environmental law, and the powers and authorisations of the Crown.

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SAUDI ARABIA SPEEDS AHEAD

Infrastructure opportunities in KSA

by Joss Dare and Faisal Baassiri

The Kingdom of Saudi Arabia (KSA) is injecting large sums of money into modernising and expanding its transport infrastructure network. As of September 2014, approximately 37 per cent of all projects currently in procurement in KSA are in the transport sector: investment in transport infrastructure is now one of the main factors driving KSA's growth after the slowdown of the construction industry in 2012.

International and long-distance domestic connections are being developed for several reasons, including:

- to accommodate the ever-increasing numbers of religious visitors to Makkah and Medina undertaking the Islamic pilgrimages of Hajj and Umra;
- to enable easier and faster connections between cities: KSA is roughly the size of Western Europe and so its major cities are a long way apart;
- to support the growing economy by facilitating the processing and/or export of natural resources, particularly reserves of phosphate and bauxite; and
- to improve connections within the Gulf Co-Operation Council (GCC) region which, in turn, will eventually lead to easier movement of freight between member states as part of a GCC-wide initiative.

This surge in investment has also focused on improving transport systems within cities and easing traffic congestion, which is both significant and increasing. The creation of modern, integrated transport networks within individual cities to improve safety and to accommodate the Kingdom's rapidly growing population (estimated to be in the region of at least a three per cent increase over the course of the next couple of years) is key to ensuring both economic growth and socio-economic stability.

Opportunities are available to foreign companies to become involved in the numerous projects planned for KSA over the coming years. This article explores the various categories of transport infrastructure opportunities and details the major projects which are under way or in development in the Kingdom.

The development in international connections

Airports

There are currently three large projects in progress to improve KSA's international airports: (i) King Khalid International Airport in Riyadh; (ii) King Abdulaziz International Airport near Jeddah; and (iii) Taif Airport near Makkah. King Khalid International Airport and King Abdulaziz International Airport were both originally built in the 1980s and are in need of expansion to accommodate greater passenger numbers and modernisation to bring them into line with international standards.

- **King Abdulaziz International Airport:** A new passenger terminal is being built at King Abdulaziz International Airport, alongside various other improvements, which will increase the airport's capacity from 13m to 80m passengers annually by its projected completion date of 2035. The main contractor is the Saudi Binladin Group who, in November 2010, won two packages of work worth US$7.2bn for the design and build of the new terminal. The work is scheduled to take place in three stages. Completion of the first phase is still expected to be some way off. The airport will also include a train station to link it to Makkah and Medina via the Haramain High Speed Rail Network (see below). This will make transport easier for pilgrims visiting the holy cities. Ashurst is working with lead adviser IFC to structure and document the O&M Concession for the airport.
- **King Khalid International Airport:** Saudi Arabia's General Authority for Civil Aviation (GACA) announced in late July 2014 that a consortium led by the German contractor Hochtief, and including India's Shapoorji Pallonji and local firm Al Nahda, had been selected for the redevelopment of Riyadh's King Khalid International Airport. The project will take place in two phases at a total contract price of US$2.9bn. The upgrade of terminals 3 and 4 is expected to take four years to complete and will be followed by the expansion of terminals 1 and 2 which should be completed in 38 months. In addition, in May 2013, GACA awarded to a joint venture of Turkey's TAV and local company Al-Arrab Contracting the estimated US$400m contract to construct a new fifth terminal. The expansion programme will increase the airport's capacity from 14m to 24m passengers per year.
- **Taif Airport:** IFC is advising GACA on the development, by way of a DBFO project, of a new greenfield airport at Taif. The airport will focus primarily on religious visitors bound for Makkah and Medina.

Rail connections within the GCC

GCC members are co-ordinating the construction of a 2,177km GCC rail network, due to be operational by 2018, which will connect the six GCC countries at a cost of US$15.4bn. This network will be used mainly for carrying freight, but it will also include some passenger services. KSA and Bahrain are also developing a 90km rail link over a new causeway – known as the King Hamad Causeway – at an estimated cost of US$5bn which will feed into the GCC rail network. KSA's transport minister Jebara Eid Al-Suraiseri announced in September 2014 that plans to build the track linking KSA to the GCC are due to begin soon.

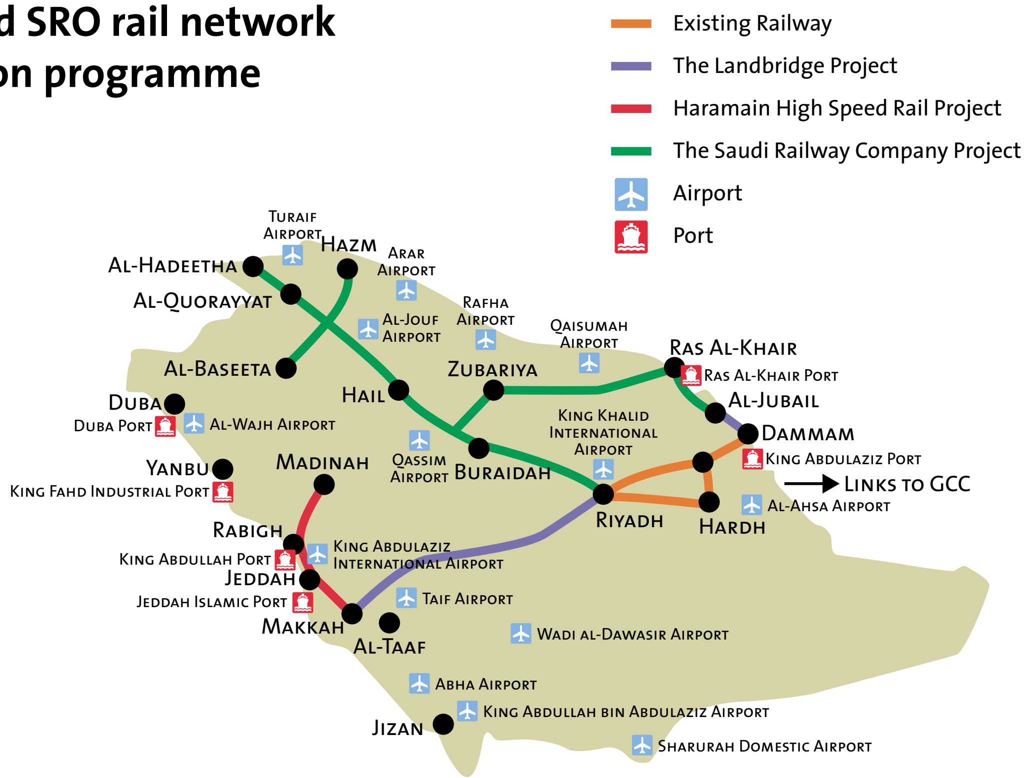
Road connections within the GCC

In September 2014, the King Fahd Causeway Authority invited contractors to submit bids for a contract to build a new island on reclaimed land to increase the vehicle capacity of the causeway linking KSA and Bahrain, with an aim of lessening congestion during peak periods.

Ports

Over the last few years, a number of contracts have been awarded for the development and expansion of ports in KSA. This includes the building of new wharfs at King Abdulaziz Port at Dammam, King Fahd Industrial Port at Yanbu and Duba Port. Most recently, in February 2014, the Saudi Ports Authority awarded China Harbour Engineering the contract for constructing three new berths at Ras al-Khair Port to enable the export of phosphate products which will be produced at Waad Al-Shamal Phosphate City from late 2016 onwards. In addition, there are plans to expand the Red Sea Gateway Terminal at Jeddah Islamic Port to increase capacity from 1.8m TEU to 2.5m TEU. Ashurst is acting for the sponsors on the financing of the expansion. Alongside these expansions, a new greenfield port – the King Abdullah Port – started operations in January 2014. The port is located roughly 100km north of Jeddah and is part of the larger King Abdullah Economic City which is being developed by a consortium headed by Dubai-based developer Emaar. The port will link KSA to the global trade passing through the Red Sea.

Projected SRO rail network expansion programme



The development in domestic connections between cities

Airports

GACA has been focusing on expanding and redesigning a number of domestic airports in addition to the development of international airports. The following projects are either currently in progress or pending:

- **Abha Airport:** In February 2014, local firm Al-Jaber submitted the lowest bid of US$480m for the contract to build a new terminal, containing 21 passenger gates, at Abha Airport. The development will be implemented in two phases with the first phase expected to increase passenger capacity from 3.5m to 5m annually.
- **King Abdullah bin Abdulaziz Airport:** A local consortium of Saudi Lebanese Modern Construction Company, Safari and Al-Subaie were awarded an estimated US$667m construction contract in May 2014 for works to be undertaken at King Abdullah bin Abdulaziz Airport in Jizan. The project includes the construction of a new three-storey passenger terminal.
- **Arar Airport:** In May 2014, a US$80m contract was awarded to local contractor Jawdat Contracting for the expansion of Arar Airport near the Iraq border. It is hoped that the construction of a new main terminal building – which will increase capacity by more than five times to 518,000 – will help to develop the area's economy.
- **Qassim Airport:** A joint venture between local firm Al-Ayuni Investment and Contracting and Turkish conglomerate Kalyon was the lowest bidder for a US$246.16m contract for which tenders were required to be submitted in August 2014. The contract will cover the construction of a new terminal which will double the capacity of the airport to 1.4m passengers per year. The contract is expected to be awarded imminently.
- **Al-Jouf Airport:** In June 2014, GACA announced plans to open bids for the construction of a new terminal and other airport infrastructure at Al-Jouf Airport. It is expected that the new terminal will increase passenger capacity from the present 175,000 to 1m each year.
- **Al-Ahsa, Al-Wajh, Sharurah, Wadi al-Dawasir, Qaisumah, Rafha and Turaif Airports:** Two separate tenders were issued by GACA in March 2014 for the redesign of seven domestic airports. The first tender was issued for Al-Ahsa, Al-Wajh, Sharurah and Wadi al-Dawasir. The second tender was for Qaisumah, Rafha and Turaif. The contracts will include the construction of new passenger terminals and runways, among other things.

Rail

KSA is the front runner in the Middle East when it comes to railway projects, despite the challenges inherent in constructing rail lines across a desert. There are three main projects under development as part of the Saudi Railways Organization's plans to expand rail infrastructure in the Kingdom:

- the Saudi Railway Company Project;
- the Landbridge Project; and
- the Haramain High Speed Rail.

There are several other projects under development or in the pipeline. For example, the Spanish firm Consultrans was appointed in September 2014 to carry out a feasibility study on a 480km high-speed line linking Dammam and Riyadh, which would see train speed increased from 180km/h to 300km/h.

- **The Saudi Railway Company Project (formerly known as the North-South Project):** Once it has been completed, the world's largest railway construction scheme, consisting of 2,750km of track, will link the Kingdom's mineral reserves in the north with cities and towns in KSA which are home to roughly one-third of the Kingdom's total population. The first phase of the project, known as the mineral route, began operating in May 2011 and allows for the direct transport of bauxite from the mine in Al-Zabirah and phosphate mined at Al Jalamid to the port at Ras al-Khair.

  Work on the second phase, a line which will mainly serve passengers, is still in progress. The line will run from north Qassim via a number of towns and cities before reaching its destination at a station near King Khalid International Airport. Ashurst is advising a consortium of Serco, Freightliner and Network Rail Consulting on their bid for this project.

Opportunities for involvement in the project still exist, with a further three phases planned. The construction of these further phases will see Ras al-Khair connected to Jubail Industrial City, a freight rail network built within Jubail, and a rail connection from Jubail to Dammam.

- **The Landbridge Project:** The second major project is the Saudi Landbridge Project which will link the Red Sea to the Arabian Gulf via a 1,200km line to cater for both freight and passengers. The line will connect the port cities of Jeddah, Damman and Jubail with the capital Riyadh through a combination of new rail track and upgrading the existing rail link between Riyadh and Dammam.

  In January 2013, US-based Fluor was awarded the project management contract and in August 2013 Italian state railway group Italferr, together with local partner Arabian Consulting Engineering Center, was awarded the design contract. These appointments marked a major breakthrough for the project which has faced many delays, primarily due to funding issues, since its launch some ten years ago. The project, once touted as a PPP, is now being financed by the state Public Investment Fund which is providing US$10bn in funding. The Saudi Railway Company has announced that it plans to invite contractors to pre-qualify in the first half of 2015 and the construction packages are expected to be tendered in late 2015, or early 2016, once the consortia have pre-qualified.
- **The Haramain High Speed Rail:** The third major project is a 440km high-speed railway, costing US$7bn, which will connect Makkah and Medina, passing through Rabigh, Jeddah and, as mentioned above, King Abdulaziz International Airport. This is the first high-speed rail line to be built in the GCC and the trains, which are being supplied by Spanish passenger train manufacturer Talgo, will run at 330km/h. The line is required to accommodate the growing number of religious visitors travelling to Makkah and Medina each year. The project is being completed in two phases: four of the six elements of the project are now complete.

Integrated transport networks within KSA's cities

In response to the rapidly growing populations in KSA's cities, five major cities – Riyadh, Makkah, Jeddah, Dammam and Medina – have developed public transportation masterplans which are all at various stages of planning and implementation. Significant progress has been made on the masterplans for Riyadh and Makkah.

Riyadh

Riyadh's 5.3m population is expected to increase to more than 8.3m by 2025. To accommodate this increase, a metro is being constructed and road infrastructure is being improved to facilitate a bus network which will interlink with the metro.

- **Riyadh Metro:** Construction of the Riyadh Metro, also known as the King Abdulaziz Public Transportation Project, officially started in April 2014 and will consist of six lines (including a connection to King Khalid International Airport), with 180km of track and 85 air-conditioned stations. Three multinational corporations were awarded the contracts in July 2013 to build the six metro lines: the "FAST" consortium led by Spanish firm FCC (lines 4, 5 and 6); the "BACS" consortium led by US firm Bechtel (lines 1 and 2); and the Arriyadh New Mobility group led by Italian firm Ansaldo STS (line 3). Overall responsibility for the project management of lines 1, 2 and 3 has been awarded to a joint venture comprising US firm Parsons International and French firms Egis and Systra. The project management contract for lines 4, 5 and 6 was awarded to a joint venture between US firms Louis Berger and Hill International. The metro is due for completion by 2019 and is expected to cost in the region of US$22-25bn. Work has now begun on the process to select the operator(s) for Riyadh Metro.
- **Road infrastructure and bus network:** Local contractor El-Seif was awarded the estimated US$107m contract to upgrade Riyadh's road network in preparation for the city's rapid bus transit system. Approximately 34km of roads will be modified and widened to accommodate the bus system which will include two circular routes, community bus lines and feeder buses to support the metro, once it has been constructed. A consortium of RATP and local firm SAPTCO were recently awarded the contract for the operation of the Riyadh bus network.

Makkah

Makkah's "Public Transport Programme" (PTP) includes the Makkah Mass Rail Transit Project (MMRT) and a smart bus system comprising rapid transit, express and feeder buses. The total cost of the PTP is expected to be US$16.5bn and is intended to accommodate the increasing number of pilgrims visiting the holy city. US company Parsons Brinckerhoff was awarded the US$93.6m project management contract for the PTP in July 2013.

- **The MMMP:** The first metro line in Makkah opened in November 2010 and was fully operational by 2011 under the name Al-Mashaaer Al-Mugaddassah Metro Project Southern Line (MMMP). The line runs only during Hajj and Ramadan and has the capacity to transport 72,000 passengers per hour, making it one of the highest capacity metros in the world. This project was constructed by, and is operated by, the Chinese contractor CRCC, with operational consultancy support from Serco.
- **The MMRT:** The city of Makkah is also well advanced with its plans to construct a general metro network across the city. Four new lines with 88 new stations and a track length of around 180km are due to be constructed. The Development Commission of Makkah and Mashaaer received bids for two packages to build the first phase of the project (two lines, 46km of track and 22 stations) from contracting consortiums in October 2014. It is understood that the tender of two project management contracts are now in progress.
- **The KAAR:** Umm al Qura for Development and Construction Company, advised by Ashurst, has been tasked with delivering the huge King Abdul Aziz Road (KAAR) project in central Makkah. This multi-billion US$ project involves the redevelopment of a central boulevard and the building of 9.5km of roads, including tunnels and two station boxes which will be used for the MMRT. The development will also include a number of high-rise buildings to house hotels, shops, offices and apartments. In September 2014, a design and build contract worth US$1.6bn was announced for the development of an initial section of the KAAR project. Huta Group and Nesma & Partners Construction are bidding for this contract.

The difficulties faced in developing the transport infrastructure

As is evident from the above, KSA is investing heavily in improving its transport infrastructure. However, the developments have not been without their difficulties. First of all, there is a shortage of workers with the skills required to develop these projects. In October 2013, it was estimated that 108,000 workers were needed for the rail projects alone. KSA has responded to these issues by building educational facilities and encouraging foreign firms to invest in vocational training. For example, Saudi Railway Polytechnic has been set up with the aim of training 1,500 students aged 18 to 21 over a five-year period. The courses will provide students with various skills ranging from mechanical, electrical and civil engineering qualifications, to train driving and health & safety qualifications. Secondly, capacity in the local construction market is increasingly being seen as an issue, given the huge breadth and scale of the projects planned.

Conclusion

KSA is one of the front runners in the Middle East in terms of its transport infrastructure strategy. New projects are being announced on a regular basis and many of the contracts have been awarded to foreign companies, highlighting the fact that the Kingdom continues to expand and modernise its transport infrastructure and that it is open to (and indeed actively encourages) the participation of foreign companies who bring to the table best practice from around the world.

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HEALTH OF THE NATION

Challenges and opportunities in the NHS

by Jane Staveley

The NHS, like any other public service, is subject to the will and whim of its public paymaster, whose objective will be to preserve a well-loved institution while, at the same time, cutting costs. This tension between keeping and cutting may throw up some interesting new opportunities for the private sector.

How will these new opportunities arise?

The NHS will be subject to three important influences over the next few years:

- political – the result of the May 2015 election;
- demographic – the impact of an ageing population; and
- financial – the estimated £8bn black hole in the NHS budget by 2020.

The impact of political change

All political parties will be expected to address their plans for the NHS in their election manifestos. Already the Liberal Democrats have flagged up mental health as a key area for them.

For so long the "Cinderella service" within the NHS, mental health services – understaffed and underfunded – are now coming to the top of the political agenda. It is recognised that the treatment of mental health needs to be placed on the same footing, in terms of resources, as the treatment of physical health. Best practice demonstrates that community-based care is more effective than hospital treatment (so-called "talking therapies"). There have been some notable successes by public service mutuals in this area.[1]

"Social diseases", such as obesity, alcohol-related illness and the inequality of access to health for rich and poor, fall within the same category. Political drivers suggest that resources will be directed towards prediction and prevention of these illnesses, rather than treatment.

Therefore, in terms of opportunities for private-sector involvement, we would expect this change in focus to:

- require an increase in larger purpose-built community facilities run by GPs or by the private sector to accommodate a wider range of health and social care specialisms to be provided within the community;
- encourage the private sector to enter into services for the most complex needs where there are high barriers

1 King's Fund report, "Priorities for the next government", 16 September 2014.

to entry. We have, for example, seen an Initial Public Offering successfully come to market last year at the most acute end of the learning difficulties sector with a rating reflecting the high demand for this service coupled with the security of a public-sector-backed payment stream;

- increase the outsourcing of specialist services for obesity, alcohol-related illnesses, dementia and age-related therapies. We would expect these services to focus on early intervention, such as expanding the requirement for statutory weight monitoring in state-maintained schools (which currently only applies in Reception year and in Year 6), nutrition and other life-skills education, and exercise facilities for the elderly. We have seen a number of outsourcing contracts for services including for children in care, health care in prisons, and frail/elderly care; and
- bring about a "sea change" in the use of technology. There will be apps for everything: for patients to keep in touch with their doctors/carers; home-monitoring equipment to sense movement (or lack of it); robots to fulfil some roles performed by carers; clothes made of heat-sensitive textiles to monitor changes in body heat; watches and other gadgets to monitor calorific consumption, alcohol consumption and heart rate, etc.

The impact of demographic change

The average age of a hospital in-patient is 80. Increasingly, the types of diseases which hospitals treat are those related to age. Such diseases seldom need to be treated in an acute hospital. The general trend is towards more community-based care to prevent, wherever possible, the revolving door of hospital stays, early discharge and re-admittance. The strategy to be implemented by the Health and Social Care Act 2012 and the Care Act 2014 is to integrate care and to deliver at scale with resulting economies.

We would expect the impact of demographic change and this legislation to:

- increase the demand for sheltered housing with wardens on call and a high level of service provision. These "evergreen villages" are not strictly health projects and tend to serve the more affluent elderly sector and so are self-financing, but such developments often require integrated or co-located health services;
- generate an awareness in the workplace of the needs of, and an increase in, an ageing workforce and how to recognise age-related diseases.[2] Such training will be rolled out across firms in the same way that diversity and other anti-discrimination training is delivered as best practice; and
- bring about the merger of health and social care budgets and commissioning to avoid duplication, cut costs and offer a one-stop-shop service, particularly for home-based services.[3] The most likely outcome of merged budgets is a further round of outsourcing of health and social care services as one combined service.

The impact of a financial deficit

The need for the NHS to find £20bn of efficiency savings has reached the stage where all low-hanging fruit has been picked. The latest prediction is that the NHS will need a further £8bn of government funding to continue to provide core services by 2020.[4] There is an urgent need for debate on how the NHS is to be funded, whether some services will need to be paid for and whether some services will lie outside the NHS's obligation to provide. Merging health and social care services and budgets may improve efficiencies but will involve a further period of dramatic change, which will come at a cost.

We would expect this to generate a need for private sector involvement, given that:

- 25 per cent of all NHS Trusts (including Foundation Trusts) are in financial difficulty, some of which have PFI

2 *Financial Times*, 27 October 2014.

3 Kate Barker's report "A new settlement for health and social care" details how this is to be funded. King's Fund, 4 September 2014.

4 National Audit Office report, "The financial sustainability of NHS Bodies", 7 November 2014.

contracts in place.[5] Various solutions have been put forward: some are resolved within the NHS family by encouraging one NHS Trust to take over a failing trust; some are bailed out financially by the Department of Health (at a cost in 2012, for example, of £1.5bn) or, in the case of a Northumbrian trust, by the local authority (see box below). Others, such as Peterborough and Stamford, are looking at ways to remain an independent going concern but to generate more income from their assets. Circle Healthcare took over the management of Hinchingbrooke Hospital in early 2012 but in January 2015 announced that it would be withdrawing from the contract, citing an unprecedented increase in A&E admissions, a lack of care places for patients awaiting discharge and a funding cut of over ten per cent.

NHS trust becomes first to buy out its PFI contract

In October 2014, it was announced that Northumbria Healthcare NHS Foundation Trust had obtained a loan from its local council to pay off the private sector provider who built and subsequently ran Hexham General Hospital. The deal, which is the first time an NHS Trust has bought out a PFI contract, is expected to save the Trust around £3m a year over the next 19 years and could prove a trailblazer for other NHS trusts and local authorities keen to extract themselves from PFI deals which no longer represent value for money. In 2012, the Department of Health gave a £1.5bn bailout to seven trusts, but many are still struggling, with the South London Healthcare NHS Trust having been put into administration partly because of its PFI obligations.

- NHS England has recently published its five-year plan. The two main features are new care models and a further disposal of surplus NHS land. From data published by the Department of Health[6] it is clear that the number of NHS land-owning bodies has reduced from 284 to 251 in 12 months, largely because of the abolition of Primary Care Trusts and Strategic Health Authorities. Disposals mean that land held by the NHS is reducing by about four per cent per annum but there is still a declared surplus of 661 hectares, plus land held by NHS Property Services Limited (NPS). Disposals generated £180m in 2012/3 and are forecast to generate £223m in 2013/4. The NHS has been instructed, as a matter of urgency, to sell off further surplus land for housing, wherever possible.[7] The remaining estate (i.e. non-surplus land) suffers from an estimated £4.047bn of backlog maintenance of which £1.373bn is critical. The NHS budget allocated £2.128bn of capital investment for 2014/5. NPS holds £3bn worth of assets (4,000 properties, mainly ex-primary care trust premises) now occupied by clinical commissioning groups. A recent report showed that NPS is operating at a loss because of rent collection arrears.[8] The NHS will need assistance in developing surplus land to be sold for housing and in managing the NHS operational estate (i.e backlog maintenance and "sweating" assets).

NHS Estate Efficiency Review

Savings of at least £1.5bn could be made through better use of the NHS estate, according to a recent report by consultants EC Harris. Figures in the report suggest that, although there has been a 61 per cent reduction in unused and surplus space in the NHS since 2008, there remains a lot more which could be done. According to the report, which is the fifth NHS Estate Efficiency Review, the health service has so far failed to make much headway in its efforts to create a more uniform estate and improve its facility management spend: *"From our analysis, the current estate has a surplus of 4.8 per cent ... by driving towards the mean average estate performance, this would equate to £1.5bn in potential savings".*

NHS Estate Efficiency Review, EC Harris, 3 October 2014.

- The NHS needs to embrace anything that can be proven to save money through efficiency savings. The private sector has the opportunity to be innovative: e.g. disseminating best practice in delivering efficiencies nationally or encouraging clinicians to come up with ideas on how to deliver a better service at less or the same cost, etc. The last thing the NHS needs is more change. It does, however, need to be offered the carrot of a better way of doing things as opposed to the stick of ever more unachievable targets in the face of surging demand and a diminishing budget.

The jury is out on the extent to which the NHS will be capable of achieving "more for less", but the private sector may hold the key to achieving the solution to what looks like, on the face of it at least, an almost insoluble conundrum.

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5 The 19 hospitals that are in financial difficulty according to the Audit Commission report (2014) are as follows: Barking, Havering and Redbridge University Hospitals NHS Trust; Barnet and Chase Farm Hospitals NHS Trust; Epsom and St Helier University Hospitals NHS Trust; George Eliot Hospital NHS Trust; Hinchingbrooke Health Care NHS Trust; Ipswich Hospital NHS Trust; Leeds Teaching Hospitals NHS Trust; Mid Essex Hospital Services NHS Trust; Mid Yorkshire Hospitals NHS Trust; North Bristol NHS Trust; North Cumbria University Hospitals NHS Trust; North West London Hospitals NHS Trust; Shrewsbury and Telford Hospital NHS Trust; Surrey and Sussex Healthcare NHS Trust; The Princess Alexandra Hospital NHS Trust; United Lincolnshire Hospitals NHS Trust; University Hospital of North Staffordshire NHS Trust; Weston Area Health NHS Trust and Worcestershire Acute Hospitals NHS Trust.

6 Hospital Estates and Facilities Statistics 2013/4. Also of interest is the fact that estate running costs have reduced by one per cent. Hard FM costs in 2013/4 were £4.4bn and FM costs £2.9bn. These costs do not include the cost of financing the estate (depreciation and cost of capital).

7 *Financial Times* report, January 2014.

8 National Audit Office report on NHS land disposals reveals that NPS is £250m in the red because of rent arrears.

TAXING TIMES

How will BEPS impact infrastructure funds?

by Nicholas Gardner

In September 2014, the Organisation for Economic Co-operation and Development (OECD), as part of its ongoing action to combat Base Erosion and Profit Shifting (BEPS), issued its report on Action Plan 6 entitled "Preventing the Granting of Treaty Benefits in Inappropriate Circumstances" (the Action Plan 6 Report). This article considers the potential implications of the Action Plan 6 Report on the OECD's ability to structure international infrastructure investment funds tax efficiently.

The BEPS project

Since the financial crisis of 2008 and the recession that followed it, increasing focus has been placed on preventing aggressive tax avoidance by multinational corporations. Governments have long promised action to tackle these practices, some of which have been described as "morally repugnant" by the UK Chancellor of the Exchequer, George Osborne.

Following the OECD Declaration on BEPS made on 29 May 2013, and endorsed by the finance ministers of the G20 nations, the OECD has embarked on a co-ordinated global action plan to tackle BEPS. The project has been split into two sets of OECD reports (referred to as "deliverables") – the first set published in September 2014 and the remainder to be published in September 2015. The 2014 deliverables address issues including hybrid mismatches, transfer pricing rules (particularly in relation to intangibles), country-by-country reporting, harmful tax practices and the digital economy. A further 2014 deliverable is Action Plan 6, which addresses abuses of double taxation treaties (DTTs) and is, arguably, the most significant of the 2014 deliverables for infrastructure funds.

> *"Fundamental changes are needed to effectively prevent double non-taxation, as well as cases of no or low taxation associated with practices that artificially segregate taxable income from the activities that generate it."*
> **OECD Action Plan on Base Erosion and Profit Shifting, 19 July 2013**

The Action Plan 6 Report focuses on preventing the abuse of DDTs and preventing the practice of "treaty shopping" which the OECD describes as an "*arrangement through which a person who is not a resident of one of the two states which have concluded a tax treaty may attempt to obtain benefits that that treaty grants to residents of these states*". Although tax avoidance by large multinational corporations is the primary target for these arrangements, funds (including those established to invest in infrastructure) potentially could be affected by the proposals, as described below.

Proposals to combat treaty shopping

The Action Plan 6 Report proposes amendments to the OECD Model Tax Convention (the Model Treaty) to prevent abuse of the treaty. The Model Treaty is generally used as the basis for bilateral DTTs entered into between sovereign states. Action Plan 6 recommends that states should have the flexibility to select which of the recommendations they implement into their DTTs, provided each state implements "a minimum level of protection" against treaty abuse and treaty shopping.

The Action Plan 6 Report provides for a limitation on benefits (LoB) provision to be added to the Model Treaty. The LoB provision is specifically designed to combat the situation where a non-treaty-resident uses a treaty-resident intermediary (such as a company incorporated and resident in the relevant treaty jurisdiction) to become entitled to the benefit of the relevant DTT. Generally speaking, the LoB will work by restricting the scope of treaty benefits under a DTT to those "qualified persons" who satisfy one of the tests in the LoB to prove that it has a sufficient connection to one of the states which has entered into the relevant DTT.

Additionally, in order to capture treaty shopping arrangements which are not caught by the LoB, the Action Plan 6 Report recommends the introduction of a principal purpose test (PPT) into the Model Treaty. The PPT will prevent a party from obtaining the benefit of the relevant DTT if "*obtaining that benefit was one of the principal purposes of any arrangement or transaction that resulted directly or indirectly in that benefit, unless it is established that granting that benefit in these circumstances would be in accordance with the object and purpose of [the relevant DTT]*". In contrast to the LoB, the test under the PPT is a subjective one. The subjective nature of this test, and the lack of certainty in the accompanying commentary, creates scope for uncertainty in its application.

As an additional measure, the Action Plan 6 Report has recommended that all DTTs include a statement in their title or preamble that the intention of the DTT is to prevent double taxation without providing opportunities for double non-taxation, tax evasion and tax avoidance. Indeed, the additional wording suggested goes as far as explicitly stating that the intention of the DTT is not to provide for treaty shopping opportunities. In addition to acting as a statement of principle, this preamble will be considered by the courts of the contacting states whenever they are asked to interpret any of the provisions in the relevant DTT.

The UK already has a number of these recommendations in existing treaties (for example, LoB provisions in the US/UK treaty, and PPT provisions in the interest and dividend articles of the UK/Netherlands treaty).

Action Plan 6 implementation options to achieve the "minimum level of protection"

States should (in addition to amending the preamble to their DTTs), amend their DTTs to include either:

1) a limitation of benefits article and principal purpose test;
2) a principal purpose test only; or
3) a limitation of benefits article and restricted principle purpose test applicable to conduit finance arrangements (or domestic law preventing such arrangements).

Impact of Action Plan 6 on international infrastructure funds

Infrastructure funds, like most other asset class collective investment vehicles, will typically be structured as transparent vehicles (such as limited partnerships) so as to avoid an additional layer of tax. Partnerships, of course, cannot benefit from double taxation treaties and most jurisdictions look through to the ultimate investor but, given the disparity of investors in such funds, it is standard practice for a fund to establish a holding company (a HoldCo) in a jurisdiction with a favourable treaty network, which will sit between the fund and the special purpose vehicles which invest directly in the infrastructure projects. The purpose of the HoldCo is to enable access to a treaty which will reduce outbound withholding taxes from the jurisdiction of the infrastructure project and, potentially, avoid any non-resident capital gains tax on exit. One of the most common jurisdictions for establishing such a HoldCo is Luxembourg, which has over 70 DTTs in force with other states relating to income and capital taxes. Ireland, Cyprus and Malta are also traditionally popular jurisdictions for establishing a tax-efficient HoldCo.

The desire to gain access to treaty benefits is common in the context of infrastructure funds, as a fund will only be viable to the extent that its tax position is no worse than the position of its investors had they invested directly. In addition, infrastructure funds by their very nature tend to be more income-producing than, say, a private equity fund where the profit will generally come in the form of a capital gain. Therefore, reducing withholding tax on annual income becomes an important economic factor. Access to these benefits – rather than seeking to engage in the type of aggressive tax avoidance which the Action Plan was intended to target – is a key aspect of fund economics.

In the original version of the LoB provision published as part of the March 2014 BEPS Report Consultation Draft (the Consultation Draft), virtually any inclusion of a HoldCo in an intermediate country (i.e. a country other than the one in which the taxpayer is resident or in which the actual infrastructure investment will take place) would have amounted to treaty shopping.

In light of the negative consultation responses received to the Consultation Draft, the Action Plan 6 Report carves out the issue of funds and collective investment vehicles (CIVs) and states that further work must be done in relation to the treaty entitlement of CIVs and non-collective investment vehicle funds, particularly given the policy considerations which apply to such investment. These policy considerations would appear to be particularly strong in the infrastructure sector, as global governments continue to use infrastructure development to stimulate economic growth and recovery.

The position adopted under Action Plan 6 in relation to CIVs is that states would be able to:

- classify CIVs as individuals and, therefore, qualified persons, in all situations;
- allow CIVs to be qualified persons subject to a potentially wide range of optional restrictions; or
- ignore completely the issues relating to CIVs, which would have the effect of denying treaty benefits to CIVs and funds in the vast majority of cases.

Non-CIV funds are almost entirely ignored in Action Plan 6, other than the statement that further work needs to be done, and there is no indication at all as to any provisions to be made for their benefit.

In light of the comments by Raffaele Russo (see overleaf), it appears likely that some provision will be made to enable contracting states to grant DTT benefits to CIVs. However, even implementing the second option above provides for a potential myriad of different arrangements under the different bilateral DTTs, and could also

> *"Effectively we carved out, for the time being, collective investment vehicles. The rules are meant to curb abusive practices but* ***should not affect situations where there is no such abuse, which may well be the case for funds*** [emphasis added]."
> **Raffaele Russo, Head of the OECD BEPS Project**

include imposing potentially onerous reporting requirements on funds regarding their ownership, which could vary from jurisdiction to jurisdiction.

In addition, it is unclear how the relevant provisions will deal with funds or CIVs which hold their investments through subsidiary companies (as in the case of the HoldCos described above). This does not appear to have been considered by Action Plan 6 and, therefore, it remains to be seen how (if at all) this potentially vital issue will be dealt with. It would appear arbitrary to deny treaty benefits simply because a fund invests through a chain of subsidiaries rather than directly, and perhaps the derivative benefits provision proposed as part of the LoB (which enables the benefits of the relevant DTT to be available in cases where the owners of a treaty-resident company which are not themselves resident in a contracting state would have been entitled to the benefits had they invested directly) could be drafted to allow the subsidiaries of the fund to access treaty benefits in such a scenario.

In addition to any specific rules for CIVs, the inclusion as qualified persons of bodies owned by a contracting state or a political subdivision of the state, may be drafted so as to incorporate sovereign wealth funds. If so, these entities, which are responsible for large amounts of infrastructure development, would still therefore be able to access treaty benefits. Funds which are set up to provide pension or similar benefits may also fall within the definition of "qualified person".

Finally, there is the ability to request that the competent authority of the source state grant access to the relevant DTT even if the investor does not otherwise qualify for treaty benefits. This can only be done if the competent authority is satisfied that the principal purpose is not to obtain tax benefits under the relevant DTT. This test is similar to the one contained in the PPT. However, leaving the eligibility to be determined by individual competent authorities is hardly likely to lend itself to the consistency of treatment for which the OECD would be hoping.

The PPT, if implemented (see above in relation to the "minimum level of protection" against treaty abuse and treaty shopping), will supplement the LoB test and may further restrict the availability of benefits under DTTs. However, there is a carve out under the PPT test for situations where, even though obtaining a tax benefit was one of the principal purposes of the arrangement or transaction, granting the benefit would be in accordance with the object and purpose of the DTT. Although the PPT is subjective, this carve out may mean that its impact on infrastructure funds is minimal as long as the fund is being structured so as not to incur double taxation, rather than to exploit an opportunity to achieve double non-taxation.

Implementation timetable

The Action Plan 6 Report was published on 16 September 2014, along with the deliverables for six of the other actions set out in the BEPS Action Plan. However, the model provisions and commentary in the Action Plan 6 Report are expressed as "drafts that are subject to improvement before their final versions are released in September 2015" on the basis that they may require some revision once the reports on the remaining eight actions set out in the BEPS Action Plan are published in September 2015 and the funds issue has been considered in further detail.

The OECD, while acknowledging that states which are parties to bilateral DTTs require flexibility in implementation of Action Plan 6 recommendations (subject to achieving the "minimum level of protection"), proposes to amend the Model Treaty as part of the negotiation of a multi-lateral instrument (MLI). This negotiation will be undertaken at an international conference which is scheduled to begin in early 2015. However, one of the issues which will need to be addressed is whether a MLI can accommodate the level of flexibility proposed in the Action Plan 6 recommendations for bilateral treaty amendments.

Given that the outstanding deliverables are not due until September 2015, it is highly unlikely that the amended Model Treaty and associated commentary containing the final product of the BEPS Report will be issued and approved before 2016.

Conclusion

The reforms to the international network of DTTs resulting from Action Plan 6 and the wider BEPS Action Plans should be significant for funds in all sectors, with international infrastructure funds being no exception. It is frustrating that the recently published Action Plan 6 expressly refers to CIV and other funds as being an area where further work will be required, possibly right up until the publication of the further deliverables in September 2015 and beyond, especially given the need for funding of infrastructure developments. Clarifying the definition of CIV funds and monitoring any provision made for non-CIV funds will be particularly important.

Participants in this sector will need to remain up to date on the progress of the remaining deliverables under the BEPS Action Plan, the further amendments to, and implementation of, Action Plan 6 recommendations and their potential implications for the structuring of international infrastructure funds, as described above. One of the key issues will be to confirm that corporate subsidiaries of infrastructure funds will have the same ability to claim treaty benefits as the funds themselves. Also, when drafting the governing documentation for new funds, consideration should be given to the provisions allocating risk and mitigating the effects of adverse changes in law following the date of the fund's formation.

Finally, infrastructure funds (and their associated industry bodies) will need to engage with other stakeholders, public sector bodies and the media in relation to both Action Plan 6 and the wider taxation debate to ensure that the benefits of continued infrastructure investment and the concerns of investors are taken into account during the process of implementing the Action Plan 6 proposals. On this point, it is worth noting that concerns voiced by the Alternative Investment Management Association following the publication of the Discussion Draft, to the effect that the original proposals would hinder investment in infrastructure and other funds, may have played a role in prompting the OECD to mark this area as one which requires further consideration.

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A LONG TIME COMING

Privatisation of the Spanish airports operator

by Gonzalo Jiménez-Blanco and José María Anarte

Aeropuertos Españoles y Navegación Aérea (Spanish Airports and Aerial Navigation) (AENA) is the largest airport operator in the world, managing 46 airports (including Madrid-Barajas and Barcelona-El Prat airports) and two heliports in Spain, and involved, directly or indirectly, in the operation of a further 23 airports worldwide.

AENA is 100 per cent owned by the state operator ENAIRE Entidad Pública Empresarial (ENAIRE). However, ENAIRE is currently in the process of selling 49 per cent of the share capital of AENA to private investors, with the Spanish Government retaining a majority stake of 51 per cent. The AENA privatisation represents one of the most ambitious projects undertaken by the Spanish Government in recent years.

Over the past number of years, AENA has been implementing a viability plan, including the refinancing of its €14bn debt, to make itself more attractive to potential private investors. In addition, the Ministry of Public Works announced its intention to reduce operational costs and to undertake the management of its airports in a more efficient manner, in order to increase the value of AENA.

According to a statement issued last year by the Minister of Public Works, between August and September of 2013 the number of passengers using AENA's airports increased by 5.2 per cent, to a total of 20m, continuing the recent positive trend in passenger numbers.

One of the main reasons for the AENA privatisation has been to enable the Spanish Government to raise funds to alleviate its public deficit. This is being undertaken at the behest of the European Commission. A few years ago, the Spanish Government attempted to privatise another of its "jewels of the crown" by promoting the privatisation of the national lottery, Sociedad Estatal de Loterías y Apuestas del Estado SA. However, this process was aborted due to market conditions. This strategy has been seen before, in 1996, when the last major wave of privatisations was launched in Spain as a result of which other Spanish public companies, such as Telefónica and Repsol, were sold to private investors.

AENA: origin of the privatisation process

On 1 December 2010, the Spanish Government announced its intention to allow private companies to take up to a 49 per cent stake in AENA, with the aim of raising €9bn. Following this announcement, the Government approved Royal Decree-Law 13/2010 of 3 December 2010 (RDL 13/2010) which governed, among other things, the privatisation and modernisation of airport services through the incorporation of a state-owned company under the corporate name of Aena Aeropuertos, S.A. (Aena Aeropuertos). The effective incorporation of Aena Aeropuertos took place on 25 February 2011, allowing the partial privatisation process to move forward.

Under the legal framework set out by RDL 13/2010 and various ancillary regulations, the privatisation process of AENA was officially launched on 30 July 2011, although with a smaller scope than originally anticipated since it was limited to the Madrid-Barajas and Barcelona-El Prat airports only. The process relating to these airports, using a concession-based model, was divided into two stages:

(i) the award of a concession agreement to each of two special purpose vehicles (SPVs) incorporated for Madrid-Barajas and Barcelona-El Prat airports (initially fully owned by Aena Aeropuertos); and
(ii) the transfer of a majority stake in each SPV to private investors, acting individually or as part of a consortium.

Seven consortia, including some of the biggest players in the industry, submitted tenders. However, the process was thwarted by a number of factors, including the high share price, concession conditions which the private sector found unacceptable, disagreement as to the allocation of risk, and difficult conditions in the financial markets. All of these factors led to the postponement of the process.

Privatisation process revisited

More than a year after its cancellation, the Spanish Government decided in 2013 to reopen the privatisation process for AENA. However, the new privatisation process differs considerably from the original in both scope and structure. While the original process was based on a concession model and limited to the Madrid-Barajas and Barcelona-El Prat airports, the new process has a much broader scope and aims to sell the share capital in AENA to private investors.

In response to a request made by AENA, on 21 October 2013, the Spanish Privatisation Consulting Council[1] (SCCP) published a report on the design of the privatisation process of AENA, proposing the creation of a group of core shareholders alongside a retail and institutional IPO (Initial Public Offering).

The aim of the privatisation is to reinforce the management of AENA, to guarantee the future sustainability of the Spanish airport system, and to stimulate the Spanish transport sector and other linked strategic sectors, such as tourism.

Under the new arrangement, the Spanish Government will retain a majority stake in AENA (51 per cent) and the remaining shares (49 per cent) will be placed in private hands through a dual-track process whereby:

- a "stable nucleus" of shareholders (Anchor Investors) numbering between two and four and selected through a two-phase restricted tender process (*Procedimiento restringido*), will hold up to a maximum of 21 per cent of AENA's share capital; and
- the remaining shares (up to the maximum of 49 per cent of AENA's share capital) will be offered for sale via an IPO.

1 Consejo Consultivo de Privatizaciones is the body which advises the Spanish Government on the privatisation process for public companies, as well as in all aspects relating to their efficiency. The reports, which are produced at the Government's request, are advisory in nature and the Spanish Government is therefore not bound by the advice contained in them.

Restricted tender process

The selection of the Anchor Investors has now been carried out by means of a two-phase restricted tender process consisting of an Invitation Phase and a Selection Phase.

Invitation Phase

Individual legal entities and consortia consisting of a maximum of three members were eligible to file invitation requests, provided each of the consortia members complied with the capacity requirements and was willing to accept individual liability for each and all of the obligations set out in the Tender Specifications for those submitting joint invitation requests.

Applicants invited to move to the Selection Phase also had to comply with the usual capacity and financial requirements for this kind of process.

Selection Phase

The Selection Phase involved the selection of the Anchor Investors from among the bidders who had passed the Invitation Phase and had thus been invited to take part in the Selection Phase.

Applicants invited to take part in the Selection Phase received, together with the invitation, the following documents: (i) tender specifications for the Selection Phase; (ii) a pro-forma bid bond; and (iii) a non-disclosure agreement (NDA) to be entered into with ENAIRE.

Once the NDA had been signed and the bid bond deposited, applicants were provided with access to a Virtual Data Room to carry out their due diligence and to prepare their bid to become an Anchor Investor.

The award criteria used to assess the bids submitted by the Anchor Invertors were as follows:

- maximum price per share or cap: this was the most important element in the assessment of the various bids which were submitted (consisting of 41 per cent of the bid assessment score);

- endorsement of the IPO and the credibility of the investor in attracting other investors to be involved in the IPO (20 per cent of the bid assessment score);
- maintenance of the investment: a minimum lock-up period of one year (17 per cent of the bid assessment score);
- premium over the IPO price (ten per cent of the bid assessment score);
- stake to be acquired: a minimum of five per cent and a maximum of 11 per cent (those offering percentages closer to the maximum threshold of 11 per cent received more points in the assessment of their bids) (seven per cent of the bid assessment score); and
- commitment period for not acquiring additional shares in the share capital of AENA, other than those awarded under the Selection Phase (five per cent of the bid assessment score).

The price payable for the acquisition of shares by the Anchor Investors is fixed by reference to the price payable under the IPO – unless an Anchor Investor has previously offered a higher price.

Anchor Investors

After undertaking the selection process referred to above on 14 October 2014, ENAIRE announced to the market that it had selected Corporación Financiera Alba (the investment arm of Grupo March), Ferrovial (which manages more than 25 airports worldwide and is currently the indirect owner of 25 per cent of Heathrow Airport Holdings Ltd) and The Children's Investment Fund, to become the Anchor Investors.

The price offered by the Anchor Investors ranged from €53.33 offered by Corporación Financiera Alba to €48.66 offered by The Children's Investment Fund. This resulted in the above investors having the right to acquire the following stakes in the share capital of AENA:

- Corporación Financiera Alba: 8 per cent
- Ferrovial: 6.5 per cent
- The Children's Investment Fund: 6.5 per cent

As mentioned above, the three investors will be in position to acquire 21 per cent of the share capital of AENA at a price to be determined, by taking into account the price fixed during the flotation process, provided that this price is not higher than the price offered by each of the investors.

IPO

Following the selection of the Anchor Investors, ENAIRE will now float a further 28 per cent of the share capital of AENA. ENAIRE has selected BBVA, Santander, Morgan Stanley, Bank of America Merrill Lynch and Goldman Sachs as global co-ordinators for the IPO. The IPO will consist of both retail and institutional tranches.

According to a spokesperson for the Ministry of Public Works (Ministerio de Fomento), AENA will apply half of the proceeds obtained from the flotation to pay down debt and the other half to distribute dividends to its shareholders, to demonstrate its pay-out policy.

Current status

Following the selection of the Anchor Investors, the Spanish Government made a decision on 31 October 2014 to postpone the IPO by a couple of months to enable an auditor to be selected to sign the comfort letter required for the prospectus which will govern the IPO. (The Spanish Government had been reluctant to allow AENA's auditor to issue the comfort letter on account of impartiality concerns.) The selection of an auditor took take place in December 2014, with EY being appointed to the role. On 23 January 2015 the Spanish Council of Ministers approved the IPO of AENA, and the prospectus for the IPO has been published on the website of the Spanish market regulator. The listing on the Madrid Stock Exchange is scheduled to take place on 11 February 2015. According to press reports, the Anchor Investors have given an undertaking to maintain the terms and conditions of their offers until April 2015.

So, an interesting few months lie ahead for the Spanish airport sector.

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A WORLD OF OPPORTUNITY

G20 and EU infrastructure initiatives get off the ground

by Catherine Clarke

According to the Organisation for Economic Co-operation and Development (OECD), an estimated US$70tn in investment is required in infrastructure globally by 2030. As a result, increasing investment in infrastructure is high on the agenda of global leaders.

Prime Minister of Australia, Tony Abbott, accurately described the situation at the World Economic Forum in January 2014 when he said: "*Developing countries need new infrastructure, developed countries need rebuilt infrastructure and almost every country is struggling to finance the infrastructure it needs*".

In September 2014, G20 Finance Ministers and Central Bank Governors agreed a Global Infrastructure Initiative to support public and private investment in quality infrastructure. This decision was well-received and consistent with the G20's ongoing efforts to address the growing infrastructure deficit.

As outlined in the G20's communique, the key objectives of the Global Infrastructure Initiative include:

- establishing a knowledge-sharing network to aggregate and share information on infrastructure projects and financing between the public and private sectors;
- addressing key data gaps which matter to investors;
- developing effective approaches to implement the voluntary G20 Leading Practices on Promoting and Prioritising Quality Investment;
- building the capacity of officials to improve institutional arrangements for infrastructure by sharing best practice approaches; and
- enhancing investment opportunities by developing a consolidated database of infrastructure projects, connected to national and relevant multilateral development bank databases, to help match potential investors with projects.

On 16 November 2014, at the G20 Summit in Brisbane, G20 leaders agreed to establish a Global Infrastructure Hub in Sydney. The Hub has been given a four-year mandate and will act as a knowledge-sharing platform between governments, the private sector, financial institutions and other international organisations to assist the implementation of the G20's Global Infrastructure Initiative.

With an annual budget of US$10m–15m, the Australian Government will be the largest financial contributor to the

Hub, along with the United Kingdom, China, Saudi Arabia, New Zealand, South Korea, Mexico and Singapore. Voluntary funding is welcomed from G20 members, non-member countries, international organisations, non-government stakeholders and the private sector. Non-members of the G20 will be able to work with the Hub and access and contribute to the information and expertise it collects.

In a virtually simultaneous development on the other side of the globe, on 26 November 2014, the European Commission launched its own Investment Plan for Europe, an initiative intended to unlock over €300bn of private and public investments over the next three years. Also known as the Juncker Plan, and the first big initiative of the recently appointed President of the European Commission, it will target infrastructure (notably transport infrastructure, education, broadband, renewable energy and energy networks) and will focus on projects that are riskier and more complex in nature.

The three key aims for the Investment Plan for Europe are:

- to mobilise public and private financing resources;
- to facilitate a pipeline of viable projects including using innovative finance instruments and providing technical support; and
- to remove barriers to investment.

In order to achieve these aims, a new European Fund for Strategic Investments (EFSI), which will be part of the European Investment Bank (EIB), will be given seed capital of €21bn for targeted investments, of which €16bn will come from the EU budget and the remaining €5bn from the EIB's reserves. The plan is for the Fund to be operational by mid-2015, following endorsement by the EIB's governing bodies. As with the G20 initiative, the European Commission will be setting up a new investment advisory hub for project promoters, investors and public authorities, to be operational by mid-2015.

Legislation to give a statutory basis to the EFSI was introduced in January 2015, with a view to its coming into force by June 2015. In the meantime, the EIB has been putting in place the arrangements for the EFSI, and project identification accelerated at an EU level. The plan is for the structure of the EFSI to allow other national promotional banks, member states and institutional investors to participate at a later date. Once the Investment Plan for Europe has been active for a year (in approximately mid-2016), heads of state and governments will review its progress.

In other related developments, the World Bank has recently launched a Global Certification Programme for PPP schemes. Together with the Asian Development Bank and the Inter-American Development Bank, the Bank has established a programme to help build national capacity to identify infrastructure needs and to develop, implement and manage projects in partnership with the private sector. Laurence Carter, senior director for PPPs at the World Bank Group, said: "*We believe this certification programme can fill an important gap in current approaches to capacity building by developing a global standard of knowledge, helping to facilitate the development of a common language on PPPs, and harmonise expectations and understanding between practitioners involved at different stages and on different sides of the PPP process*".

The move comes as the UN also looks to develop better practices for countries preparing PPP initiatives, with the United Nations Economic Commission for Europe (UNECE) creating a set of guidelines for PPP units to follow, which will see compliant authorities given accreditation. Overseen by the UNECE, the purpose of the plan is to develop a scheme by which "zero tolerance to corruption" principles are implemented by awarding countries' PPP units and other agencies with a certificate for compliance.

These initiatives demonstrate how governments right across the world have now fully woken up to the benefits of harnessing private sector finance in building and maintaining public sector infrastructure. Hopefully each of these plans will bear fruit in the coming years, creating an ever more vibrant worldwide project finance marketplace.

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STOP PRESS:

Top tier rankings for Ashurst's Transport and Infrastructure team

Ashurst's Transport and Infrastructure practice has been recognised as a premier global adviser in the leading legal directories, **Chambers & Partners** and **Legal 500**. Published annually, these guides provide unbiased commentary and insight into regional legal marketplaces.

Here is a brief overview of our recent rankings from across the globe:

United Kingdom

Our London-based Transport and Infrastructure team has been acknowledged in both Chambers and Legal 500 for its breadth across the sectors and for a reputation of acting on consistently high-profile and complex projects globally.

Our Infrastructure PFI/PPP practice has been listed in the top tier for the tenth year running by **Chambers UK 2015**. The chapter highlights Ashurst's broad array of domestic and international work and our "*impressive reputation for flagship projects in the healthcare, education, defence, waste and transport arenas*". Many of our partners in the department have also been singled out as "*leading individuals*".

In the Rail sector, we are the only firm to be awarded top tier status in each of Franchising, Projects & Infrastructure and Rolling Stock.

Ashurst has also maintained a top tier position in the **Legal 500 UK 2014** rankings for Infrastructure (including PFI & PPP), where we are described as a "*top tier*" team, who "*go the extra mile*", with "*strength-in-depth at both partnership and associate level*".

Middle East

In **Legal 500 UAE 2014**, the Projects and Energy team are listed in the top tier, while our partners are regarded as "*more practical than those in other similar firms*".

Asia-Pacific

We also hold a top tier ranking in **Chambers Asia Pacific: Japan** for Projects & Energy. Equally, as an illustration of our market leading top tier position for Construction, Projects & Energy, the **Legal 500 Japan 2014** guide claims that Ashurst "*has a strong practice in Japan, and its consistent approach to the Japanese market has enabled it to reap the benefits*".

Our growing Australian Infrastructure practice is praised as a tier two adviser in the Australian chapter of the **Legal 500 Asia-Pacific 2014** guide. This accolade builds on the global reputation of the firm for providing clients with a joined-up excellent service.

Commenting on the firm's performance, Global Head of Infrastructure, Mark Elsey, said:

"These global rankings have further established Ashurst's position within the global elite group of international law firms. Across our global network, we welcome these rankings as recognition of the service we are able to provide to our clients. Our lawyers are always ready to build upon our reputation as a globally excellent firm and a leading adviser for all Transport and Infrastructure-related work".

For full details of the rankings and text summaries, visit the Chambers website at chambersandpartners.com and the Legal 500 website at legal500.com.

Global League Table rankings

In addition to our position in the legal directories, Ashurst has also been ranked highly in one of the most prominent infrastructure league tables – **InfraDeals** – who have published their annual results for 2014. The exclusive results show Ashurst's ranking as third for Legal Advisers by value in the global project finance market for 2014, with a total value of US$34,751m for the 40 accredited deals captured in their report, which places us in fifth place for our deal count. These league tables provide a valuable reference for the project finance and infrastructure community by measuring investment and financing activity in the development of infrastructure assets.

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