The Prospects of Introducing the Private Finance Initiative in the UAE Construction Industry

الأبعاد المستقبلية لمبادرات تمويل القطاع الخاص لصناعة الإنشاءات في دولة الإمارات العربية المتحدة

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Abstract

Private public partnerships have assumed new dimensions through a process of constant evolution in synchronisation with modern economic challenges. Private finance initiative has emerged as the leading choice for public ventures requiring private involvement especially in the more advanced economies. In recent years, there has been an overwhelming move to take up private finance initiative as a means to facilitate governance through the involvement of the private sector. Third party involvement has comprised in large part on infrastructure provision as well as some service provision. Given the changing trend in public procurement and service provision, countries such as the UAE are looking towards private finance initiative as the leading method to provide for a demanding populace as the global economy tends to slow down. However, the UAE tends to face a host of challenges not the least of which are its aging economic structures required to support private finance initiative. Research has been carried out to investigate the various social, political and economic challenges that may contribute to and hamper the progress of private finance initiative in the UAE. Results show an encouraging realisation of the need to move towards private finance initiative although structural issues in the social and political arena remain. In turn, social and political issues tend to hold back economic reformation required for the progress of private finance initiative. The current state of the UAE's economy has the potential to install private finance initiative with essential yet gradual social, political and economic reformation.

موجز

اتجهت بدائل مشاريع المشاركة الحكومية مع القطاع الخاص نحو منحى جديد يتمثل في مواكبة متزامنة مع التحديات الأقتصادية الحديثة. وتعتبر مبادرة التمويل الخاص في مقدمة هذه البدائل المفضلة لدى الاقتصاديات المتطورة عالميا. وقد تم تبني هذه المبادرة بسبب الرغبة لدى الأطراف ذات الصلة زيادة مشاركة طرف ثالث في عمليات الحوكمة التي تشارك في إدارة هذه المشاريع المشتركة بين القطاعين الخاص والعام. أن وجود طرف ثالث في عملية المشاركة بين القطاعين كان له أثره الفعال في نجاح كثير من مشاريع البنية التحتية بالإضافة إلى تحسين جودة الخدمات العامة. ومواكبة للتغير في طريقة المشتريات الحكومية وتقديم الخدمات للجمهور، فأن دولة الأمارات العربية المتحدة شأنها شأن الدول المتطورة بدات تفكر جديا في الأخذ بهذا المنحى في تنفيذ مشاريع البنى التحتية وتقديم الخدمات الحكومية وخاصة في مثل الظروف المالية الصعبة في هذه الفترة. ولكن الأمر ليس بالسهولة للدولة لكي تخطو في هذا المجال حيث ينبغي لها أن تهيء بعض الأصلاحات الأساسية في التشريعات التي تنظم مثل هذه المبادرة. وعليه فأن البحث يتطرق إلى مختلف التحديات الأجتماعية والسياسية والأقتصادية والتي يمكن أن تؤثر في نجاح هذه التجربة في الدولة. إن النتائج الأولية للبحث تشجع نحو المضي قدما في تطبيق مبادرة التمويل الخاص بالرغم من أمكانية حدوث ردات فعل إجتماعية وسياسية غير مرغوب فيها وهي لا شك ستكون معوقا نحو تطوير هذه المبادرة في الدولة. إلا ان التطبيق التدريجي لمثل هذه المبادرات يمكن أن يخفف من الآثار الجانبية المصاحبة لعملية التنفيذ ويعين على تطوير الأنظمة اللازمة سواء على الأصعدة السياسية والقانونية والأجتماعية.

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List of Abbreviations

BOT	Build, Operate, Transfer
COAG	Council of Australian Governments
DBFO	Design, Build, Finance, Operate
FNC	Federal National Council
FSC	Federal Supreme Court
FVC	Financial Vehicle Corporation
IA	Infrastructure Australia
NHS	National Health Service
PFI	Private Finance Initiative
PPP	Public Private Partnerships
SoPC	Standardisation of PFI Contracts
SPE	Special Purpose Entity
SPV	Special Purpose Vehicle
WTO	World Trade Organisation

1 Chapter One – Introduction

1.1 General Background

Private finance initiative (PFI) can be seen as a subset of Public Private Partnerships (PPP) that is geared to deliver public projects by utilising and involving the private sector's capacity[1]. In its simplest terms, PFI refers to the utilisation of private money for public purposes using a chalked out framework[2]. It is typical for PFI projects to encompass both the provision of infrastructure and services to the general public. Recent years have seen massive growth in PFI around the world in general and in Great Britain, Spain and Australia in particular[3].

The PFI way of delivering on public infrastructure and services was first widely implemented in the United Kingdom after which it was replicated by Australia and Spain. The impetus behind PFI emerged from the wider drive towards privatising finances as part of the overall neoliberal agenda. Recent decades saw the waning capacity of governments worldwide to provide for public infrastructure and services[4]. The consequent gap or vacuum created is assumed by PFI mechanisms that ensure that public infrastructure and services are delivered.

Another major push factor behind PFI is the promotion of efficiency using private initiatives. It comes as no surprise that the private sector tends to be more efficient than the public sector and PFI banks on this distinction to ensure optimal delivery in terms of both cost variance and schedule variance. The success of PFI can be judged from the fact that in the United Kingdom alone, some 563 PFI projects had been completed with a capital value of 35.5 billion pounds by 2003[5]. Similar to the concerns of efficiency are claims of increased accountability in PFI projects. It has been argued time and again that PFI encourages better and more transparent

[1] Alan Richards and John Waterbury, *A Political Economy of the Middle East* (Boulder, Colorado: Westview Press 2008)
[2] Allyson Pollock, *NHS Plc: The Privatisation of Our Health Care* (London: Verso 2005)
[3] J Barlow, J K Roehrich, and S Wright, 'De facto privatisation or a renewed role for the EU? Paying for Europe's healthcare infrastructure in a recession' Journal of the Royal Society of Medicine 103 (2010)
[4] N. Gregory Mankiw, *Principles of Economics* (New York: McGraw Hill 2007)
[5] David Corner, 'The United Kingdom Private Finance Initiative: The Challenge of Allocating Risk' OECD Journal on Budgeting 5(3) (2006)

procurement measures which provide for greater accountability[6]. However, critics argue that PFI provides less value addition for the same fiscal expenditure over the longer run though there is little evidence as yet to support such contentions fully[7].Research Problem

The Middle East collectively amounts to strong economies that were driven by oil based growth. The recent slowdown of global economic giants such as the United States, Western Europe and now China has impacted the Middle Eastern economies too. Like other governments around the world, Middle Eastern governments have solely been responsible for the provision of public infrastructure and services[8]. However, the turndown in economic output in these economies signals of problems to come as average growth in GDP around the Middle East hovers at a meagre 4%[9] [10]. Weak diversification attempts around the Middle East have meant that in hard times the governments have few options to either cut down on service or infrastructure provision or increasing financial availability[11].

Given the current circumstances and the wasteful spending in public finances in the Middle East due to poor management practices[12], the need of the hour is to switch over to PFI in the Middle East. The contention behind this change would be to promote greater efficiency and accountability in public sector projects around the Middle East. Even though the PFI solution seems realisable but there are structural as well as other hurdles that hamper the growth of PFI in the Middle East. The proposed research will examine these problems to discover the applicability of PFI to the UAE.

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[6] James Barlow and Martina Koberle-Gaiser, 'Delivering Innovation in Hospital Construction: Contracts and Collaboration in the UK's Private Finance Initiative Hospitals Program' California Management Review 31(2) (2008)

[7] Mark Hellowell and Allyson M. Pollock, *The PFI: Scotland's Plan for Expansion and its Implications*, (University of Edinburgh 2007)

[8] Clement Henry and Robert Springbord, *Globalization and the Politics of Development in the Middle East* (Cambridge: Cambridge University Press 2001)

[9] Marcus Noland and Howard Pack, *The Arab Economies in a Changing World* (Washington, D.C.: Peterson Institute for International Economics 2007)

[10] David Waugh, *Geography, An Integrated Approach* (Nelson Thornes Ltd. 2000)

[11] Hassan Hakimian and Jeffrey Nugent, *Trade Policy and Economic Integration in the Middle East and North Africa: Economic Boundaries in Flux* (New York: Routledge 2004)

[12] Long Le-Hoai, Young Dai Lee and Jun Yong Lee, 'Delay and Cost Overruns in Vietnam Large Construction Projects: A Comparison with Other Selected Countries' KSCE Journal of Civil Engineering 12(6) (2008)

1.2 Research Questions

The proposed research aims to answer the following research questions:

1. What prospects exist for implementing PFI in UAE?
2. What kind of factors tend to favour the implementation of PFI in the UAE?
3. What kind of factors tend to discourage the implementation of PFI in UAE?
4. How can major stumbling blocks to PFI implementation in UAE be overcome?

1.3 Aim and Objectives

The aim of the proposed study is to determine if PFI could be implemented in UAE to reap benefits such as increased efficiency and greater accountability. This aim is augmented by the following objectives:

1. To assess if PFI could be implemented in UAE to deal with public projects;
2. To examine what kinds of factors encourage and discourage PFI implementation in UAE;
3. To create strategies based on findings for overcoming any hurdles to PFI implementation in UAE.

1.4 Research Methods

The proposed research will utilise both qualitative and quantitative methods for the purposes of data collection and analysis of the study. The contemporary PFI frameworks around the world with special emphasis on the United Kingdom and Australia will be analysed in detail to delineate their structure and functions through a literature review. This will be carried out utilising available materials such as books, journal articles, official websites, reports, audits etc. Once the salient features of these PFI frameworks become clear, they will be superimposed to the UAE situation to form a comparison. Various hurdles such as structural economic problems, political and social peculiarities and the role of religion in the economy in UAE will be analysed in order to see how and why PFI in its current form is viable or not. The analysis will be carried out by dissecting the underlying cause of PFI discouraging factors in UAE and seeing how they apply to UAE. This will be carried out by analysing various forms of literature such as books, journal articles, official economic figures and the like in order to produce a wholesome and credible picture.

The findings of the literature review from the above will be utilised to create a broad set of problems and catalysts for PFI implementation in the UAE. In order to discern if the qualitative findings from above are supported by people involved in the respective sectors in the UAE, surveys will be administered. The surveys will be created based on the findings of the qualitative section areas. A survey will be drafted and administered to government personnel in the Ministry of Finance, Public Works and Foreign Investment and to various project managers working in the construction sector in order to discern their concerns for PFI in UAE. The survey will be constructed so that qualitative findings from the literature review can be translated into discernible quantitative responses from the survey respondents based on the responses to the survey's questions. The results of the survey will be tabulated to see how many industry personnel agree or disagree with various catalysts and inhibitors for PFI implementation in the UAE.

1.5 Significance of the Research

The proposed research will provide for an all out account of various kinds of factors that are inhibiting the growth of PFI in UAE. Less than optimal performance in public spending in UAE is causing billions of dollars of losses to the economy. The need of the hour is to promote efficiency and transparency to provide for sustainable development.

1.6 Dissertation Outline

The dissertation will be divided into six chapters that are described below.

Chapter One will provide for a background to PFI, its evolution and current form being applied worldwide. This chapter will also delineate the research problem along with the proposed research questions. Among other things, this chapter will establish the scope of the overall study.

Chapter Two will provide for major structural differences in the economic structures of nations utilising PFI and UAE. The evolution and current form of economic structures including the role of governments in market regulation will also be considered.

Chapter Three will look into legal issues that confront UAE as well as United Kingdom and Australia. The political issues will consider issues that are commonly applicable as well as issues that are unique to UAE or to the United Kingdom and Australia.

Chapter Four will examine the legal issues that tend to affect UAE's economy. Legal peculiarities unique to UAE will be brought to light to consider how these may inhibit the growth of PFI.

Chapter Five will bring together the various factors elucidated from previous chapters and will analyse them to discern how they encourage or discourage PFI implementation in the UAE. Survey results will also be presented in this chapter to gauge PFI applicability in UAE.

Chapter Six will look into the consolidated factors inhibiting PFI in UAE to elucidate methods for its application and Findings.

Chapter Seven will provide conclusion, recommendations and future research areas.

2 Chapter Two – PFI Structure, Practices and Evolution

2.1 Introduction to Private Finance Initiative (PFI)

Public private partnerships (PPPs) are designed to incorporate private funding into public programs using a regulated framework. It is typical for PPP frameworks to involve the government as a regulation mechanism while the private sector provides for finance as well as development and in some cases for operation of public utilities[13]. The private finance initiative (PFI) framework can be seen as a subset of the larger PPP framework. The contention behind PFI is to involve the private sector to provide finance for public projects. This framework also relies on the private sector to design, build and in some instances operate public sector utilities and services. The involvement of the private sector is part of the wider agenda of neo liberalisation and privatisation aimed to improve the efficiency and accountability of public spending[14].

One of the chief drivers of the PFI mechanism is that the procurement of infrastructure and services for the public sector relies on the private sector such that the requirements are dictated by the public sector. The biggest difference between PFI and other PPP frameworks is the utilisation of private finance which is underwritten by the public sector according to its requirements[15]. The private sector may be involved beyond the financing by allowing the private sector to design, build and finally operate the planned public infrastructure or services. In certain cases, PFI allows the public sector to transfer its assets to the private sector for management such as healthcare facilities[16]. Hence, PFI could involve any set of public sector projects that require private finance as well as other private sector inputs whether the project concerns:

a. new developments of infrastructure or services; or
b. transfer of existing infrastructure and services.

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[13] J Barlow, J K Roehrich and S Wright, 'Europe Sees Mixed Results From Public-Private Partnerships For Building And Managing Health Care Facilities And Services' Health Affairs 32(1): 146-154 (2013)
[14] J Barlow, J K Roehrich, and S Wright, 'De facto privatisation or a renewed role for the EU? Paying for Europe's healthcare infrastructure in a recession' Journal of the Royal Society of Medicine 103 (2010)
[15] J Barlow, J K Roehrich, and S Wright, 'De facto privatisation or a renewed role for the EU? Paying for Europe's healthcare infrastructure in a recession' Journal of the Royal Society of Medicine 103 (2010)
[16] J Barlow, J K Roehrich, and S Wright, 'De facto privatisation or a renewed role for the EU? Paying for Europe's healthcare infrastructure in a recession' Journal of the Royal Society of Medicine 103 (2010)

2.2 PFI Practices

The public sector delineates specifications for any infrastructure or service needs and invites private investors to provide their proposals for fulfilment. Depending on the size of the undertaken project, it is common for private investors to group together as consortiums to provide their proposals. It must be taken to note that PFI is used typically for large projects where it is not possible for a single private investor or service provider to provide the required set of objectives. In order to deal with the large scope of PFI projects, it is common for private sector parties to group together for the length of the project including the proposal stage[17].

The common umbrella used by private sector parties is typically known as a Special Purpose Entity (SPE), Special Purpose Vehicle (SPV) or as a Financial Vehicle Corporation (FVC) within the European Union[18]. For the purposes of this paper, the consortium of private sector parties will be labelled as a SPV.

2.2.1 SPV Dynamics

The SPV umbrella is created as a legal entity for temporary purposes to deal with a specific set of objectives. The primary contention behind SPVs is to reduce the risk exposure of private businesses involved in large projects. The use of SPVs to insulate the larger firm from fiscal risk exposure is a standard practice used around the world although there have been cases of its abuse as well such as the Enron scandal[19] [20]. In the case of PFI arrangements, various different private investors band together in order to create a SPV which is used to enter into contractual arrangements with the public sector. The SPV framework allows the larger private investors to move both finance and assets to the SPV for management and operation[21].

[17] European PPP Expertise Center, 'Bankability' <http://www.eib.org/epec/g2g/i-project-identification/12/123/index.htm> accessed on 7 March 2013
[18] European PPP Expertise Center, 'Bankability' <http://www.eib.org/epec/g2g/i-project-identification/12/123/index.htm> accessed on 7 March 2013
[19] Bethany McLean and Peter Elkind, *The Smartest Guys in the Room* (New York: Portfolio Trade 2003)
[20] Bala G Dharan and William R Bufkins, *Enron: Corporate Fiascos and their Implications* (New York: Foundation Press 2004)
[21] Gary B Norton and Nicholas S Soueles, *The Risks of Financial Institutions* (University of Chicago Press 2007)

The SPV created for PFI purposes is not owned by a single private investor but rather by a number of different private parties that may include builders, operators and financers[22]. The financers may include fiscal institutions such as banks or other individual private investors. The SPV arrangement allows the private parties to bring together various forms of expertise to bolster efficiency and accountability. The consortium is designed so that finance for the project is available; the construction team is at hand and the operators of the project see through the entire effort before assuming responsibilities[23]. Moreover, it is also possible for SPVs to transfer project responsibilities to other parties as long as negative cost and schedule variances do not take place. Amendments to already agreed upon contracts may also be taken up using SPVs at any particular stage in the project[24]. It is common for SPVs to charge for their services when acting as intermediaries between end consumers and service providers[25]. A typical SPV framework delineated by Swaffield and McDonald is shown below for reference.

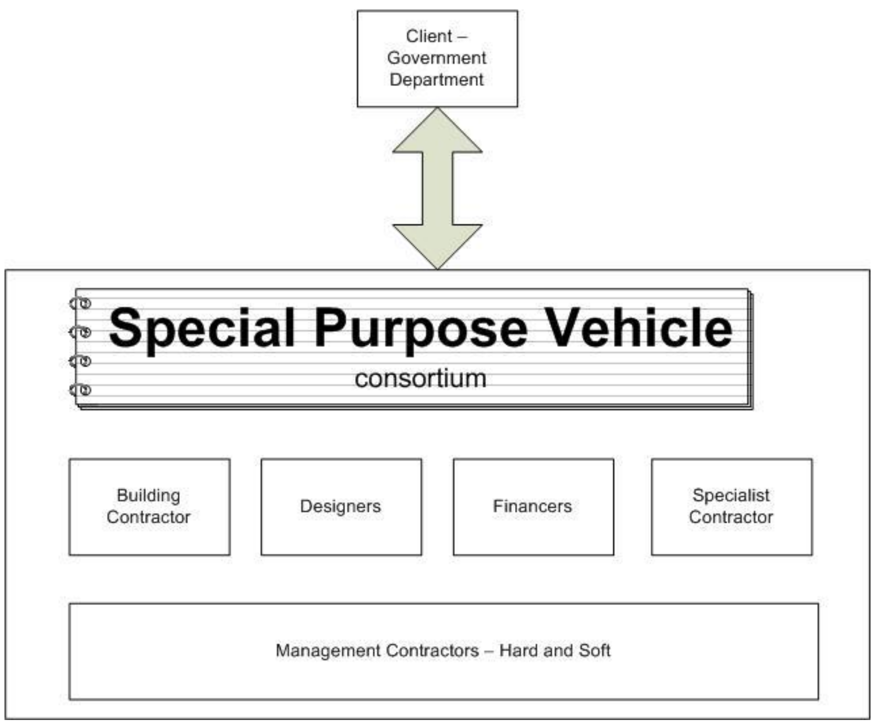

Figure 1 - SPV relationship to the overall PFI framework. Source: Swaffiled and McDonald (2008).

[22] J Zheng, J K Roehrich and M A Lewis, 'The dynamics of contractual and relational governance: Evidence from long-term public-private procurement arrangements' Journal of Purchasing and Supply Management 14(1): 43-54 (2008)
[23] Vinod Kothari, *Securitization – The Financial Institution of the Future* (John Wiley and Sons 2006)
[24] Saleh N Neftci, *Principles of Financial Engineering* (Academic Press 2008)
[25] Jim Packard, 'PFI deals "not doing good job"' Financial Times, <http://www.ft.com/cms/s/0/89b9f926-7886-11dd-acc3-0000779fd18c.html> accessed 8 March 2013

2.2.2 Contracting Period

PFI contracts vary widely in terms of the overall contracting period. Most PFI projects tend to last between 20 and 30 years given the scope and size of the projects[26] [27]. In contrast, certain PFI projects may also last up to a decade only[28] while others may last up to 35 years[29]. The particular nature and service characteristics of a project tend to decide the overall contracting period. The initial contracting period decided upon can be altered with the mutual consent of all involved parties at any stage through the utilisation of the SPV.

2.2.3 Public Sector Specifications

For any PFI project to emerge, the public sector must provide some kinds of specifications for infrastructure or services. Typically, it is common for the public sector to constitute some authority in order to provide the specifications which are better known as output specifications. The work of the SPV in turn depends on the output specification since the involved private parties are actually trying to achieve whatever is spelled out in the output specification. Most PFI contracts provide that if the private consortium is unable to meet any of the demands set forth in the output specifications, then it is liable to payment reductions, fines or any other kinds of mutually agreed upon action. This continues until the requirements spelled out by the output specification are met[30]. In case that a consortium fails to meet output specifications repeatedly, it is up to the public sector interface to remove the consortium by another consortium or to take ownership independently. The existing consortium is paid for its services and the project ownership is changed[31].

[26] Partnerships UK, 'Case Study : Norfolk County Council - Street Lighting PFI Project', <http://www.partnershipsuk.org.uk/PUK-Case-Study.aspx?Project=11832> accessed 8 March 2013
[27] Partnerships UK, 'Case Study: Neath Port Talbot Hospital' <http://www.partnershipsuk.org.uk/PUK-Case-Study.aspx?Region=Wales&Project=11683> accessed 8 March 2013
[28] Partnerships UK, 'Case Study: Lewisham Schools Catering Services' <http://www.partnershipsuk.org.uk/PUK-Case-Study.aspx?Region=London&Project=11209> accessed 8 March 2013
[29] Partnerships UK, 'Case Study: Redevelopment of the Treasury Building, Government Offices Great George Street (GOGGS)' <http://www.partnershipsuk.org.uk/PUK-Case-Study.aspx?Region=London&Project=11418> accessed 9 March 2013
[30] Saleh N Neftci, *Principles of Financial Engineering* (Academic Press 2008)
[31] L M Swaffield and A M McDonald, 'The contractor's use of life cycle costing on PFI projects' [2008] Engineering, Construction and Architectural Management 15(2) 132-148

2.2.4 Termination of Project

PFI contracts may be cancelled by either the public sector interface or the private sector interface though the process is intricate and requires significant tinkering. Given the trend in PFI contracts, it is more common for public sector interfaces to cancel PFI contracts rather than for private sector interfaces to cancel PFI contracts. The public sector may remove the PFI contract given the non performance by the private consortium. In contrast, the private sector has large amounts of finance involved which cannot be expunged with immediate effect from any project without a net loss in profits and investment. For this reason, it is more common for the public sector to expunge the private sector consortium if non performance or under performance occurs rather than the other way around[32].

A number of PFI contracts have been cancelled over the years for non performance and under performance though other commercial reasons may also contribute to cancellation of contract[33]. The particular means of contract termination tend to depend on the exact nature and scope of the project as well as the involved capital and any contract terms. As presented in the diagram below, some PFI projects tend to have rather complex inter party relationships leading to unique contract termination schemes. The particular PFI contract referenced below is for the National Physical Laboratory[34] where underperformance of the overall consortium led the public sector to terminate the contract with the Laser consortium[35].

It must be noticed however that the entire contract need not be cancelled as some of the private parties can be retained such as the lending parties. In order to do so, the public sector interface could force the private consortium to disband into its components as shown below. The underperforming or non performing contractor can be reimbursed and let go while other private contractors can be retained in a new PFI environment[36]. This form of contract termination tends

[32] Vinod Kothari, *Securitization – The Financial Institution of the Future* (John Wiley and Sons 2006)
[33] Tom Fitzpatrick, 'London Underground ditches PFI deal' HVN Plus, <http://www.hvnplus.co.uk/news/london-underground-ditches-pfi-deal/8634540.article> accessed 11 March 2013
[34] National Audit Office, 'The Termination of the PFI Contract for the National Physical Laboratory: Full Report' London: The Stationery Office (2006)
[35] Committee of Public Accounts, 'The Termination of the PFI contract for the National Physical Laboratory' London: The Stationary Office (2007)
[36] National Audit Office, 'The Termination of the PFI Contract for the National Physical Laboratory: Full Report' London: The Stationery Office (2006)

to provide flexibility compared to conventional contracting arrangements where the contracting party has to be let go completely rather than in parts.

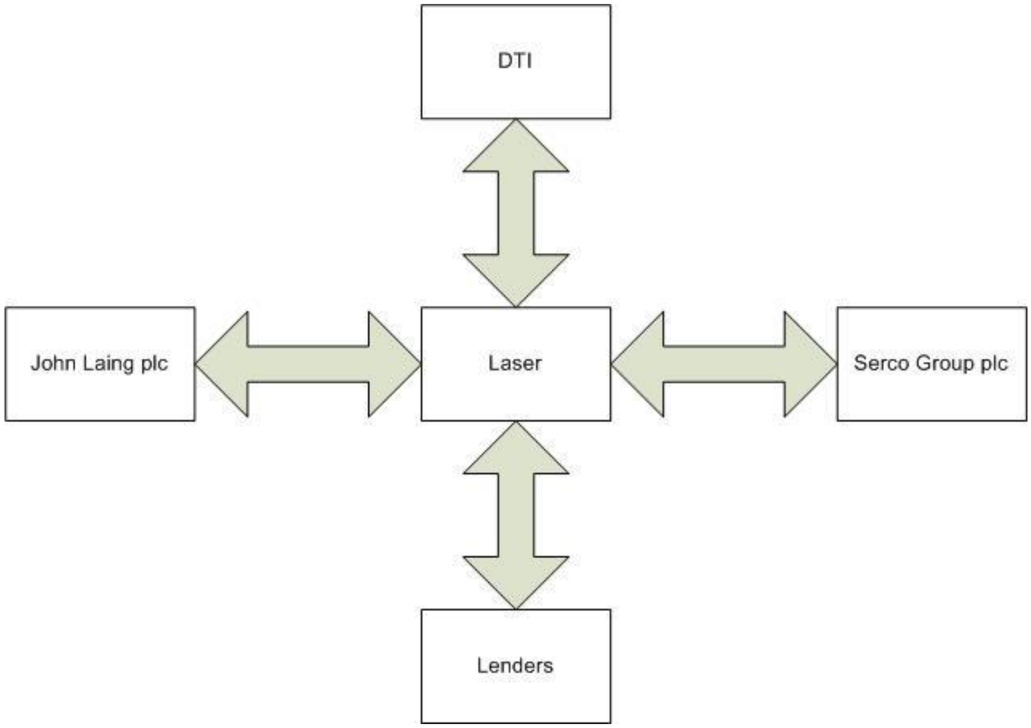

Figure 2 - Various relationships between the public sector and the private sector for a typical PFI contract that was cancelled for non performance. Source: National Audit Office (2006).

2.2.5 Project Financing Methods

Funding for PFI projects has originated from a number of different sources over time. Most PFI projects were funded using two major sources of funding: senior debts and bonds[37]. It is typical to find that large projects are funded using bonds while smaller projects are funded through the use of senior debt. In addition, it has to be kept in mind that bonds offer lower rates of return compared to senior debt based loans. Since bonds are typically provided for by the government, so the return policies are not that aggressive. In contrast, senior debt is provided for by banks which pursue far more aggressive designs for return of capital including higher rates of return on investment[38].

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[37] Stationary Office, *Private Finance Projects and Off-balance Sheet Debt: 1st Report of Session 2009-10* (London: Stationary Office 2010)
[38] Duncan Cartlidge, *Public Private Partnerships* (Routledge 2006)

Practice shows that before the 2008 global economic crisis, it was more common to see PFI deals being financed by bonds rather than by senior debt. However, after the 2008 global financial crisis, it has become more common to find senior debt as the primary method of financing in comparison to bonds. It could be argued that the economic crisis has curtailed project size as well as open market investment so that PFI financing is now dependant on banks more than on bonds[39].

2.2.6 Project Financing Concerns

As a PFI project develops, the amount of risk entailed tends to change over time. At the very start of the project, especially at the start of the construction phase, the risk entailed by any project is highest. As the project progresses, the amount of risk tends to decrease especially at the end of the project when the construction has gone to completion. It needs to be taken to note that risk is highest at the start of the project and that is when financing is essentially required. The higher rates of risk at project start mean that the early financers tend to charge heavily for the use of their capital. In addition, it is typical to find a consortium of investors so that risk is distributed so that no single party is exposed alone to risk. A typical PFI financing methodology is presented for explanation.

[39] Akintola Akintoye, Matthias Beck and Cliff Hardcastle, *Public Private Partnerships: Managing Risks and Opportunities* (Wiley 2008)

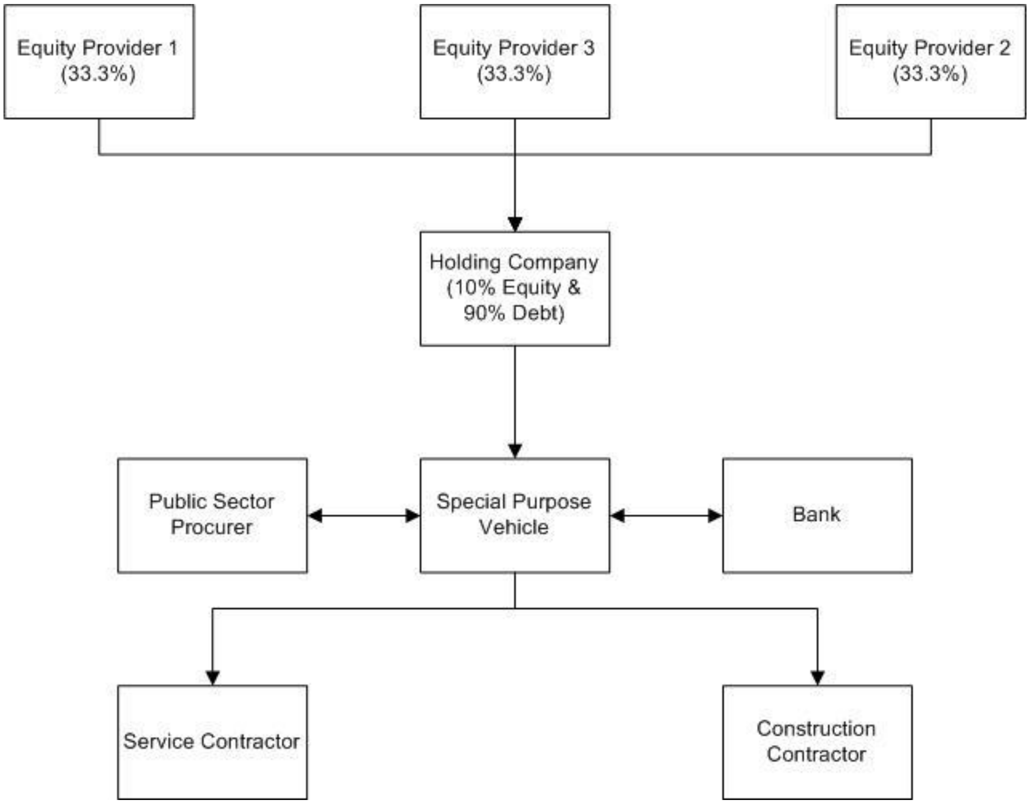

Figure 3 - Financing scheme used in order to lower the risk entailed by typical PFI projects. Source: Istemi, Iqbal, Pamela and Caral (2012).

The diagram above makes it clear that PFI funding like other forms of PPP funding is undertaken by a number of different investors shown in the top most tier. The shared investment is then handed over to a holding company that tends to represent the interest of the involved parties. The holding company in turn tends to create a SPV in order to limit the risk exposure of the actual investors as shown above. The multiple levels of protection provided to investors allow greater investor confidence and also ensure that project failure can be arrested at more than one level. This in turn promotes better project survivability since the project is backed by multiple horizontal and vertical levels when it comes to finance[40].

*2.2.6.1 **Refinancing***

It is common for PFI projects to get refinanced over their lifecycle. As mentioned before, risks are higher at the start of the project than at its end so it is common for cheaper loans to be

[40] Istemi Demirag, Iqbal Khadaroo, Pamela Stapleton and Caral Stevenson, 'The diffusion of risks in public private partnership contracts' [2012] Accounting, Auditing and Accountability Journal 25(8) 1317-1339

procured at the end of the project. Again two different options are available to deal with the refinancing concerns namely being bonds and senior debts. Bonds are utilised where the project size is large enough to make sense of such investment means while senior debts are acquired for smaller projects. A combination of both means of financing may also be utilised as well. It could be possible to acquire bank loans in order to support construction activities and bonds could be used as an option to finance the long term running expenditures. The initial investors tend to make a significant profit when projects are refinanced since the repayment terms for the acquired capital changes sizably. The benefits derived from refinancing have to be extended to the public sector or the applicable government authority as well in most cases[41].

2.2.6.2 <u>Repayment</u>

Any agents providing finance for PFI projects such as banks or bonds are repaid in the longer run by the initial investment consortium. The consortium in turn depends on the payments that it received from the public sector over the entire lifecycle of the project. Private investors are more likely to invest in PFI activities since there is little chance that large public sector organisations would come to a default. This encourages investment in PFI projects by promoting investor confidence. The rate at which repayment occurs tends to depend on the services provided as per specification by the investment consortium. The better the service provision by the operator, the sooner the repayment occurs since profit levels are optimised. On the other hand, if the operator is wasteful there are little chances that profit levels would be optimised and this would lead to larger repayment cycles. On another note, it must be kept in mind that repayment is more likely in PFI projects than in other forms of investment given the lower overall risks involved. The better repayment history of PFI projects compared to repayment histories in the private sector mean that investors are more ready to invest in PFI projects than elsewhere[42].

[41] Stationary Office, *Update on PFI Debt Refinancing and the PFI Equity Market* (London: Stationary Office 2006)
[42] Herbert Robinson, Patricia Carrillo, Chimay J Anumba and Manju Patel, *Governance and Knowledge Management for Public Private Partnerships* (Wiley 2009)

2.3 Evolution of PFI around the Globe

The fiscal cliffs of the seventies and the eighties forced many governments around the globe to look for alternative means of public procurement. During this period, many developed nations experienced massive hikes in their public debts on account of macroeconomic changes. The only real option that could be looked into was to encourage the only other sector with major investment potential – the private sector. In the very start, investment was encouraged for large infrastructure projects alone but not for service provision. However, over time the evolution of PPP in general and the evolution of PFI in general has seen the inclusion of services to the investment options available to private investors under PFI[43].

The evolution of PFI on a global scale can be attributed to around two decades of development and experimentation to arrive at a workable mechanism. Initially, PFI like much of PPP was considered to be of no cost to the public but this position was later abandoned as more evidence became available. PFI evolved from such dispositions to assume the current shape where several private investors form a private consortium to take care of infrastructure and service provision for the public sector[44]. PFI has been evolving, is evolving and will continue to do so such that PFI's evolution will depend on economic structures and their compositions that affect different economies in different ways.

In addition to nations using PFI after the fiscal cliffs of the seventies, certain nations were moving towards PFI proactively. For example, France was already building a number of infrastructure projects such as motorways, hospitals and prisons back in the sixties. This trend continued into the seventies and assumed solid ground after the fiscal problems of the seventies[45]. Other than France, both Italy and Spain were following similar ideas to incorporate private investment into the public sector as early as the seventies using infrastructure provision as the mainstay of PFI projects[46]. In order to bring about the various economic problems and obstacles surrounding UAE's move into PFI, this research will look into the evolution of PFI in the United Kingdom and Australia in order to see what factors supported PFI's growth and

[43] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)
[44] Dominic Robertson, *See-Through Modelling: A technical blueprint for financial modelling using lessons learned from PFI* (Harriman House 2013)
[45] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)
[46] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)

development. This learning will be used in order to generate findings on what economic obstacles, whether structural or otherwise, exist to hamper PFI's growth in the UAE.

2.3.1 United Kingdom

2.3.1.1 Early Decades

The United Kingdom had begun to move towards PFI as a means of fiscal provision for public sector works. The transition towards PFI in the seventies remained fluid but produced certain important findings that led to the development of the Ryrie Rules[47]. Throughout the eighties, the collaboration between public and private enterprise was undertaken using guidelines provided by Ryrie Rules. According to the Ryrie Rules, private finance was only to be used in the public sector if two major conditions were satisfied, which were:

1. private capital can only be utilised for public sector projects if it is proven that such a mode of financing would prove to be more cost effective when compared to a wholly public sector funded project;
2. the particular investment being carried out by the private sector should be an independent provision of public sector infrastructure or services rather than being an addendum.

Ryrie's Rules were given precedence over other methods of decision making for inclusion of private investment in public sector works. Ryrie's second rule has been ignored by some decision makers when it was felt that the situation did not favour such outcomes and that additions to existing public works by the private sector were required[48]. In addition, Ryrie's second rule has another implication – the value at which private investments are reduced should apply equally to public expenditures too. A number of policy makers and decision makers argued that Ryrie's second rule posed as a great obstacle to obtaining private funding for public sector works. Eventually, the United Kingdom Treasury abolished Ryrie's second rule in 1989. Consequently, any privately funded public projects did not need to pursue similar value reduction models which in turn encouraged private investment in PFI.

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[47] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)
[48] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)

2.3.1.2 The Nineties

The nineties served as the major stabiliser for the PFI evolution process in the United Kingdom. Throughout the nineties, two major reviews of the PFI process were undertaken by the public sector to optimise PFI application to PPP projects. In addition, the nineties saw a wave of standardisation being carried out in the PFI arena that was marked by a development of relevant guidelines, procedures, processes and for a renewed emphasis on the creation of value for money in PFI projects[49]. Ever since the Ryrie Rules, the emphasis had been on the cost effectiveness of the project being delivered through PFI means but the nineties changed that to place emphasis on value creation for the longer run. The longer a PFI project creates value as an infrastructure or service provision, the greater are its chances for overall success and for creating greater investor confidence in the overall PFI process[50].

2.3.1.3 The 2000 Decade

The post 2000 scenario saw the development of PFI into a structured and integral part of governance rather than as an auxiliary device as in the past. The various policies for PFI were consolidated such that integral structures of governance were introduced to both support and espouse PFI on various fronts. The major developments throughout the noughties included[51]:

- Treasury Taskforce Policy section was converted into a more permanent Office of Government Commerce (OGC);
- Technical advisory for the Treasury Taskforce Policy section was moved over to Partnerships UK which was created specifically for this purpose;
- Personnel policies were experimented with such that workers were employees of the public sector but were being managed by the private sector;
- Various contract terms and other pertinent standards were given a concrete form under the *Standardisation of PFI Contracts* (SoPC) in 2003-04;
- Project evaluation was codified using *The Green Book* introduced in 2003. According to the new system, every project under the PFI framework was to be evaluated either after

[49] Dominic Robertson, *See-Through Modelling: A technical blueprint for financial modelling using lessons learned from PFI* (Harriman House 2013)
[50] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)
[51] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)

the construction phase or at any other point in time afterwards in the lifecycle of the project;

- Housing development under the National Health Service (NHS) and the Housing Corporation received guidelines for best practices.

Overall, it could be said that the post 2000 period provided PFI in the United Kingdom a large boost. The decade emphasised on the value for money from PFI projects as well as on the transfer of risk between involved parties. The various policies and standards developed in the nineties for PFI were implemented and improved upon in the noughties to provide the current framework of PFI in the United Kingdom. It must be taken to account that the evolution of PFI in the United Kingdom represents an intricate process that has been fashioned by a number of factors including economic concerns[52].

2.3.2 Australia

Australia's PFI framework has grown tremendously after the eighties and currently has the reputation for one of the world's most efficient and transparent PFI schemes[53]. The delivery of infrastructure and services in Australia's PFI sector is significant given that it covers diverse areas ranging from roads, airports, rail systems to prisons, schools and hospitals. Australia's PFI sector is just as involved in the creation of social infrastructure and services as it is in the creation of economic infrastructure and services[54].

The PFI framework in Australia can be traced back to the eighties with projects such as the Sydney Harbour Tunnel. However, PFI remained restricted in Australia given a wide variety of challenges it faced from legislative barriers. Before the nineties, several legislative barriers prevented the private sector in Australia to invest in the public sector in large part. The part played by the private sector in the public sector was available in Australia but was restricted to certain niches alone. Following the nineties, legislative barriers were removed systematically in Australia in order to encourage investment from the private sector for providing public sector

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[52] Dominic Robertson, *See-Through Modelling: A technical blueprint for financial modelling using lessons learned from PFI* (Harriman House 2013)

[53] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

[54] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

infrastructure and services[55]. The evolution of Australian PFI can be classed into two distinct phases namely:

- Pre 2000 scenario when economic projects were open for private investment;
- Post 2000 scenario when economic and social projects were open for private investment.

The evolution of niches where private sector investment was allowed in Australia over the last few decades is represented in the diagram provided below:

Pre 1990s – 1993	1994 – 1997	1998 – 2000	2001 – 2002	2003 – 2010
Economic Projects			Economic and Social Projects	
Water	Water	Water	Defence	Defence
Roads	Power	Power	Prisons	Hospital
	Prisons	Rail	Hospitals	Schools
	Seaports	Airports	Seaports	Convention center
			Airports	Courts
			Roads	Roads
			Schools	Water
				Waste
				TAFE College Training
				Housing
				Ports and terminal
				Rolling stock
				Sports complex

Figure 4 - Evolution of the Australian PPP market. Source: JETRO (2010).

[55] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

The nineties witnessed the evolution of new legislation to replace older doctrines through acts such as the:

- National Rail Corporation Act (1992);
- Roads Act (1993);
- Airports Act (1996);
- Telecommunications Act (1997).

The basic contention behind such legislation was to offer the private sector greater flexibility to invest in public works. The major areas reformed under the acts mentioned above and other such acts were issues relating to ownership concerns, service provision terms, leasing conditions etc. The nineties provided the legal framework for Australia to expand on its PFI framework in the noughties[56].

The post 2000 decade witnessed large developments in Australia's PFI sector where developments were spearheaded by the Victorian government. The PPP framework evolved under the Victorian government placed particular emphasis on[57]:

- Greater cost efficiency in the PFI framework when compared to pure public sector development;
- Lower negative cost variance in the PPP framework;
- Risk analysis and minimisation;
- Seamless collaboration between design, construction, management and final service provision.

The post 2000 decade also witnessed significant movements in other Australian regions and territories such that significant legislative changes occurred. The contention behind the changes remained to introduce private investor friendly PFI mechanisms. Over time, various forms of horizontal and vertical developments in different Australian regions were combined in order to create a singular PFI system. This development is better known as the Council of Australian Governments (COAG) and was created. Various Australian regions and territories still have their own PFI frameworks with some differences but these are all eventually linked up

[56] Janine O'Flynn and John Wanna, *A new era of public policy in Australia?* (ANZSOG 2008)
[57] Allen Consulting Group, *Performance of PPPs and Traditional Procurement in Australia* (Allen Consulting Group 2007)

to COAG to provide a centralised measure[58]. In addition, an advisory council labelled as the Infrastructure Australia (IA) was created in 2008 to provide advice to local, territory, state and commonwealth governments at various levels.

The framework for PFI mentioned above is represented at various levels in order to bolster centralisation without compromising on the localised freedoms of public sector bodies. The federation of Australia is represented by a National Minister for Infrastructure who is augmented in his functions by a Coordinator General. This model of governance has been replicated in most Australian states in order to promote PFI friendly mechanisms for PPP development and growth. Each state with the mentioned system has an Infrastructure Minister who is augmented by the Coordinator General. In addition to other responsibilities, the Coordinator General serves as the central focus of contact for the entire system[59].

Additionally, the Australian PFI model is strictly centred on the principles of Design, Build, Finance, Operate (DBFO) alone. This stands in contrast to other PFI models such as the Japanese Build, Transfer, Operate (BTO) model.

2.3.3 Japan

Japan's PFI framework derives itself from the pioneering United Kingdom PFI framework but presents a number of restrictions in its implementation. The basic changes required to enact PFI frameworks were legislative in nature and the first major development occurred in 1999 with the passage of the PFI Promotion Law[60]. The initial PFI Promotion Law was revised in 2001 and this spurred growth in the PFI niche but the growth cannot be termed as massive when compared to other PFI changes around the globe. The current scope of the Japanese PFI niche is restricted to small projects with fiscal investments of between AUD $61

[58] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)
[59] Institute for Public Policy Research, *Building Better Partnerships: The Final Report from the Commission on Public Private Partnerships* (Institute for Public Policy Research 2001)
[60] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

million and AUD $365 million only[61]. In addition, the current PFI framework in Japan is limited to social infrastructure projects such as schools, hospitals, government buildings etc.

The Japanese example is also differentiated from that of the United Kingdom and Australia because of its reliance on the BTO model alone. This in turn means that the risk transfer in Japans' PFI framework is limited since private investors have been restricted to construction and financing alone. It has been observed that Japan's implementation of PFI is both cost and schedule efficient but legal restrictions of scope such as those mentioned above tend to reduce the size of the overall PFI market. The smaller size of the Japanese market has ensured that larger international and local investors have stayed out of the PFI sector and its development and growth[62].

Another major shortcoming of the Japanese PFI model is the lack of centralised coordination between various public sectors and their demand for PFI. The current Japanese development in PFI is on a as is basis with no particular emphasis on any particular public sector niche for PFI growth and development. The randomised nature of Japan's PFI growth model has already begun to show signs of stress and wear. Japan's PFI market is characterised by multiple small capital projects that local investors can easily deal with. Consequently, Japan's PFI growth has encouraged local investors to step up while international investors have chosen to stay out of the Japanese PFI market due to project size concerns. The small size of Japanese investors in the current Japanese PFI market has meant that growth on the part of the investors has been relatively obscure. The large number of projects out for the taking in the Japanese market has stopped attracting even local investors since there are no long term prospects for growth. The year wise growth of PFI projects in the Japanese market provides a reflection of the current problems of the Japanese PFI sector. The diagram below clearly shows that the Japanese PFI sector witnessed massive growth in the early noughties but the growth has slowed down in the late noughties on account of discouraged local PFI investors[63].

[61] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)
[62] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)
[63] Fumitoshi Mizutani, *Regulatory Reform of Public Utilities: The Japanese Experience* (Edward Elgar Publishing 2012)

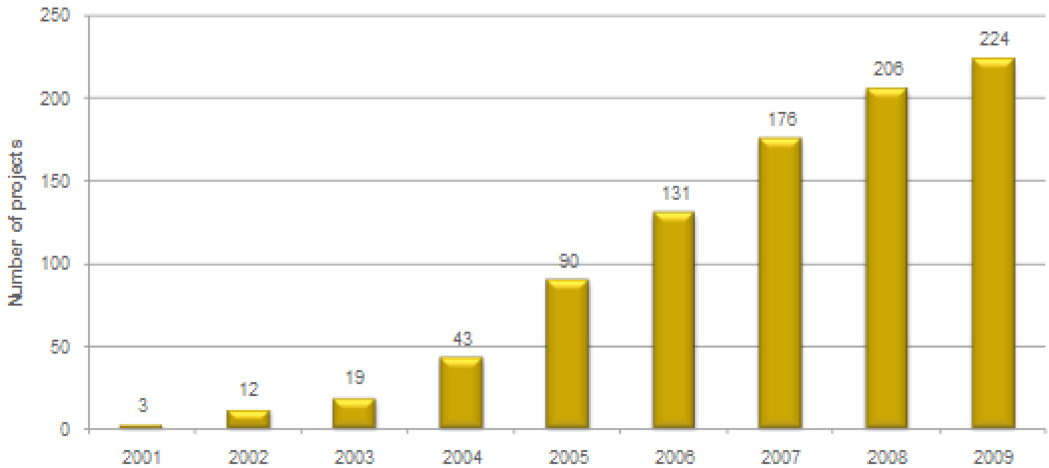


Figure 5 - Operational projects in the Japanese PFI sector classified by year[64].

Private investors are subjected to the BTO model that forces them out of the PFI process right when the project is about to become profitable. The local investors in the PFI market are not allowed to provide services except for a very limited nature of services, most of which are restricted to the construction phase alone. The lack of service provision in the PFI framework is keeping out new investors and is discouraging current investors from going too far into the PFI niche. Consequently, Japan's PFI market has begun to show signs of stress and strain although it is comparably a new PFI market. Local investors are leaving the market and there are no foreign investors to take up their place. Investment in the PFI sector is also being discouraged by the Japanese government on account of various taxation structures and accounting policies that discourage long term equity based investments in any kinds of projects at all[65].

Japan's situation is also peculiar given the intricacies of the legislative and the administrative frameworks for public procurement. There are three different levels of public procurement that can be classified as[66]:

- Local;
- Prefectural;
- National.

[64] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)
[65] Eur, *Far East and Australasia 2003* (Routledge 2002)
[66] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

Given also the fact that PFI mechanisms in Japan are limited to infrastructure provision alone, there are two different levels of infrastructure legislation that apply to the PFI sector. These are[67]:

- Local (Local Autonomy Law);
- National (National Property Law).

In order to deal with such complicated public procurement structures, the Japanese government has undertaken menial reformation at best. The major legislative changes in Japan with regards to PFI promotion have been[68]:

- Act on Promotion of PFI;
- Public Services Reform Act;
- Designated Manager System.

The limited legislation to support PFI promotion and growth in Japan has meant that major legislative obstacles have remained in place to discourage PFI growth and development. When the overall legislative framework in Japan is analysed, it becomes clear that private investors are neither allowed to own nor allowed to operate any form of public infrastructure. There are exceptions to restrictions on the private sector to own and operate public infrastructure as provided in the table below:

[67] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)
[68] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

Legislation	Details
Railway business law	Railway business participation has been opened to private investors historically.
Road transportation law	Regional and national government can use private contractors but a government body does the regulation.
Road law	- The road law gives wide powers to regional governments for change and addition. - Private sector is involved in construction and maintenance.
Aviation law	Entities may manage airports with final regulation and airport maintenance resting with the governemnt regulator.
Port law	Ports may or may not be managed by private entities depending on governmental regulation.
City Park Law	Park regulation is restricted to national and regional governments. Private sector involvement is limited and tightly regulated.

Figure 6 - Public Property Act (PPA) guidelines and allowed private sector involvement in Japan's public sector[69].

[69] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

3 Chapter Three – Legal System

3.1 Comparison of Legal Structures

3.1.1 Representative Government

The nations utilising PFI in its various forms successfully are typically representative forms of government. The political dimensions of PFI are important in terms of delivering PFI as a viable solution in the modern economy. The United Kingdom has a democratic form of government that has evolved over centuries[70]. Similarly, Australia has a representative form of government that has evolved as a dominion to the United Kingdom[71]. Japan also displays a representative form of government, though the move to representation is most marked after the Second World War[72].

The demand and the need for PFI arise only when the constitutionally elected representative government finds itself tied down by fiscal constraints. The growth and later the emergence of PFI in the seventies were marked by representative governments looking for methods to finance themselves without causing public outrage. The fiscal tie down led the governments in the Western hemisphere to consider new partners for funding public projects including the private sector[73]. The requirement to address the needs of the people by any means forced the respective governments to seek new methods to finance the public sector. However, in a non-representative system, such as the UAE, there is no such apparent need. A comparison of the UAE and other governments from advanced nations would reveal stark contrasts in terms of obligations to the people at large.

A look at the current governance reveals that the seven emirates making up the UAE nominate their singular representative from the royal family out of whom one person is chosen to

[70] Niall Ferguson, *Empire: The rise and demise of the British world order and the lessons for global power* (New York: Basic Books 2004)
[71] Lindsay Marsh, *History of Australia: understanding what makes Australia the place it is today* (Greenwood: Ready Ed Publications 2010)
[72] Donald Denoon and Mark Hudson, *Multicultural Japan: palaeolithic to postmodern* (Cambridge: Cambridge University Press 2001)
[73] Allen Consulting Group, *Performance of PPPs and Traditional Procurement in Australia* (Allen Consulting Group 2007)

lead the UAE. The only thing close to a parliament is the Federal National Council (FNC), which has forty members who are partially nominated and partially elected[74]. Given the fact that PFI was designed in order to promote efficiency and accountability in public sector spending, the UAE has little need for such measures given the lack of pressure from its governance structure. The direct consequence is felt in the economy at large where PPP has only taken off slightly with limited projects such as the Dubai Roads and Transport Authority, the Abu Dhabi Waste Management Programme, the Abu Dhabi Education Authority etc. only[75].

3.1.2 Centralised Measures versus Decentralised Measures

The implementation of PFI around the world on a national scale provides for one commonality – PFI measures are put into operation on a centralised scale. In the United Kingdom, PFI has been implemented as a policy measure of the central government and not as an initiative of the local governments[76]. The Australian experience with PFI has been similar. The PFI scheme came to Australia in the form of Partnerships Victoria whereby PFI was implemented in Victoria only[77]. The nascent success of the initiative in Victoria meant that the central Australian government took the initiative from a regional scale to a national scale with immediate effect. Policy making and implementation in regards to PFI is now carried out in Australia by the central government that ensures that PFI policies are uniform throughout the country. In the case of Japan, the government has strict control on the PFI process which is reflected in the tight regulatory control of the central government on PFI processes. The central Japanese government exerts an overbearing influence on the PFI policy making and implementation areas such that it dissuades foreign investors from entering the Japanese PFI market[78].

In contrast, the situation in UAE is entirely different. The UAE government is composed of seven different emirates that pursue slightly different policies with respect to PFI. The PFI

[74] Library of Congress, 'United Arab Emirates -- Government and Politics' (Library of Congress 2013) <http://lcweb2.loc.gov/cgi-bin/query/r?frd/cstdy:@field%28DOCID+ae0052%29> accessed 11 April 2013
[75] Simmons and Simmons, *PFI/PPP* (London: Simmons and Simmons 2012)
[76] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)
[77] Price Waterhouse Coopers, *The value of PFI: Hanging in the balance (sheet)?* (London: Public Sector Research Center 2010)
[78] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

process is more facilitated in certain emirates than in others. At the current time, it is apparent that Abu Dhabi leads the PFI process which is evident from the character of projects being undertaken under a PFI umbrella in Abu Dhabi. While other emirates in the UAE are pursuing public infrastructure provision projects in large part, Abu Dhabi has undertaken both infrastructure provision as well as service provision projects[79]. The largely varied nature of projects being pursued in different emirates in the UAE reflects that PFI policy making and implementation differs from one emirate to the other.

In the current situation in the UAE, investors tend to shirk away especially from smaller PFI projects given the relative levels of complexity in operating in various emirates. The lack of centralised efforts directed at PFI implementation mean that investors find it difficult to move between emirates in order to take up PFI projects. As a direct consequence of this fact, it is noticeable that PFI tends to proceed at different pace between different emirates. The emirates of Abu Dhabi and Dubai lead the PFI implementation process in the UAE while the smaller emirates are still not onboard for PFI implementation. The current political structure in the UAE means that central policy making and implementation can only occur if the leaders of the seven emirates agree to the subject policies. The growth and development of PFI in Abu Dhabi and Dubai along with the absence of PFI in other emirates indicates that there exists a certain divide in the ruling class over the PFI issue[80]. It may be possible in the future that all emirates take up PFI measures when the success of PFI becomes evident from the examples of Abu Dhabi and Dubai.

[79] Simmons and Simmons, *PFI/PPP* (London: Simmons and Simmons 2012)
[80] Simmons and Simmons, *PFI/PPP* (London: Simmons and Simmons 2012)

4 Chapter Four – UAE Legal Environment

4.1 Legal Factors

4.1.1 Legal Opposition to Empowering Foreign Investors

The UAE region is seen as investor friendly given the presence of tax free and duty free zones. However, it must be kept in mind that the UAE government is only investor friendly as long as local involvement in the investment is ensured. The current investment laws in the UAE make it mandatory for local investors to be involved in any investment scheme. Moreover, foreign investors cannot own more than 49% of any company's stock. This rule ensures that local investors remain superior to foreign investors under all circumstances. In a similar manner, foreign investors find myriad limits placed on their ownership of land and stocks.

Business ownership in the UAE is limited by non tariff barriers placed on investments. The most common forms of such barriers include agency based restrictions, sponsorship needs and distributorship requirements[81]. In case that a business wants to expand outside of the free trade zones into the UAE, the business needs to have a UAE national acting as the business sponsor. Additionally, the UAE national involved could have the status of an agent or distributor too. Although the UAE is bound by its agreements with the World Trade Organisation (WTO) to allow free market policies but there seems to be little movement in this direction. There are a number of laws in the drafting stage[82] but there seems to be little else going on to ensure that investors, especially larger investors, enter the UAE market liberally.

Currently UAE has shielded its local markets from foreign investor entry by using the following legal entry barriers:

- Federal Companies Law;
- Federal Industry Law;
- Commercial Agencies Law;

[81] Bureau of Economic and Business Affairs, '2012 Investment Climate Statement - United Arab Emirates' (US State Department 2012) <http://www.state.gov/e/eb/rls/othr/ics/2012/191258.htm> accessed 11 April 2013
[82] Bureau of Economic and Business Affairs, '2012 Investment Climate Statement - United Arab Emirates' (US State Department 2012) <http://www.state.gov/e/eb/rls/othr/ics/2012/191258.htm> accessed 11 April 2013

- Government Tenders Law.

Out of all these laws, the Federal Companies Law is seen as the most reprehensible for foreign investors. Under the subject law, any company established in the UAE must exhibit a minimum of 51% ownership by a UAE national or by a company owned by a UAE national. Interestingly the same law mandates that profit sharing may be carried out in any decided apportionment without any regards to the overall ownership structure[83]. This in turn makes it clear that UAE’s social norms do not allow for foreign investors to be seen as business owners. There is some speculation that in the future business ownership outside of the free trade zones would be increased to 100% but currently progress on this front seems slow. The recent turndown in the global economy has forced UAE to reconsider its business ownership laws like much of the region. However, progress has remained slow in amending such laws given the fact that the government has little need to consult a parliament or to get legislation passed otherwise to amend such legislation. The inertia experienced by the UAE government in changing the subject law stems from popular opinion. The government is unwilling to take action to amend such laws believing that such amendments in law might lead to popular opinion developing against the government. Though such a course of action may be socially and legally viable but there is little doubt that such a course of action does not favour PFI growth and development.

[83] UAE Government, *Federal Law No. (8) of 1984 as amended by Federal Law No. (13) of 1988 Commercial Companies*

5 Chapter Five – Survey Methodology

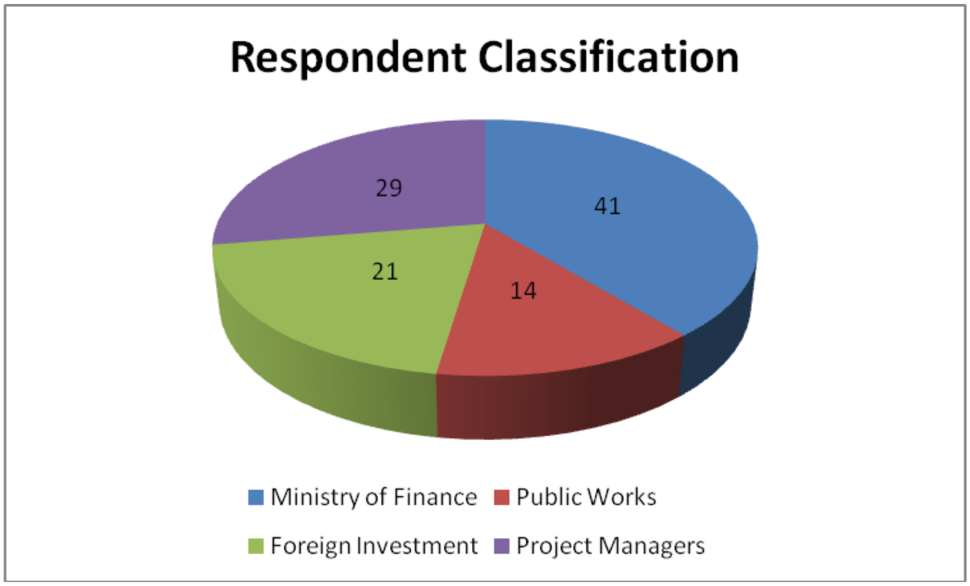
5.1 Survey Methods

In order to deal with the quantitative portions of this research, a comprehensive survey was designed and administered to a number of officials and industry personnel dealing with public and private sector projects. The contention was to precipitate factors from the qualitative research and to test them against responses from the quantitative survey results. Survey design, administration and analysis are discussed in greater detail below.

The survey was designed to be as short and comprehensive as possible so that maximum validation could be achieved while using the lowest amount of time of the respondents. Most of the respondents are busy government officials and business personnel so expecting such respondents to provide large amounts of time for surveys would have been unrealistic. A total of eighteen questions were embedded in the survey and the overall design was kept minimal so that the respondents would require less than ten minutes to fill out the entire survey.

The survey was administered to government personnel in the Ministry of Finance, Public Works and Foreign Investment and to various project managers working in the construction sector in order to discern their concerns for PFI in UAE. A total of 134 respondents were contacted by phone and email for their consent to fill out the survey forms. In response to the consent of respondents, the survey was created online and links to the survey were sent online to the email addresses of the respondents. The respondents were provided with around three weeks of time to fill out the survey forms. The results of the survey forms were tabulated real time as the inputs of the respondents began to arrive.

Out of a total of 134 respondents, 21 respondents failed to respond at all to the survey while another 8 respondents filled out incomplete surveys. Completed surveys were received from a total of 105 respondents. The 105 respondents who completed the survey forms were distributed as shown in the diagram below:



Most of the respondents were aged between 30 and 45 years of age. The average age of the respondents was 34.3 years with only 7 respondent's age being under 30 years. The average education level of the respondents was at least a bachelor's degree. The project managers surveyed for this research tended to possess masters and doctorates as well. The government officials surveyed for this research possessed at least a bachelor's degree in their relevant field of work. All of the respondents for this research had more than five years of experience on their hands at the time of the survey.

5.2 Privacy Policy

In order to protect the identities of the respondents, the online survey was designed not to capture the incoming link that directed the respondents to the survey through their email. The privacy of the respondents was ensured so that professional problems may not arise for the respondents.

6 Chapter Six – Findings

6.1 Literature Review Findings

6.1.1 Differences in Economic Structures and Market Regulation

6.1.1.1 Economic Immaturity and Regional Cooperation

UAE was still developing in the seventies as PFI was taking root in the rest of the world especially the developed world. The UAE was only beginning to discover the large oil and gas deposits it contained while nations such as the United Kingdom had already begun to experiment with native forms of PFI. In addition, regional inclinations in the Middle East do not support the utilisation of PFI in the UAE unlike Europe where United Kingdom's leap into PFI was supported by neighbouring nations such as France, Spain and Italy[84]. The large experiment base provided by nations in Europe meant that various nations implemented and learned from their and other PFI experiences. The case of the UAE is unique as other economies in the region are unwilling to progress towards PFI which means that the UAE will have to struggle more in order to come to terms with a workable PFI arrangement.

6.1.1.2 Cost Effectiveness Concerns

Another area affecting PFI implementation in the UAE concerns cost effectiveness. UAE can only utilise private capital if its cost effectiveness can be determined properly. In case that the use of private finance is not cost effective, there would be little point in utilising such a scheme of investment as per Ryrie's Rules[85]. Since the government of UAE has a large amount of cash to spend each year, it can easily provide for liquid cash investments that are cheaper compared to private investments by banks and other fiscal institutions. The fact that cheaper government capital is always available in the UAE tends to discount the use of private finance for public sector works in the UAE. However, given the significant rises in inflation in the UAE in recent years and the looming economic crisis implications, the government will be hard

[84] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)
[85] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)

pressed to pursue private investment in the future. The current situation of UAE is comparable to the economic conditions of developed nations in the aftermath of the fiscal cliffs of the seventies. UAE has the scope to learn from the mistakes of nations that have already experimented and developed PFI as a viable investment path for public sector infrastructure and services provision.

6.1.1.3 Value for Money Debate

PFI has only seen implementation where there were strong calls for value for money. UAE has relatively lax and weakly enforced rules and guidelines for certain areas in the construction industry. This is all the more true for projects that are being pursued by UAE nationals in the shape of contractors or employers. The lax standards in use tend to undermine the data required to evaluate the value for money produced by a project under PFI. The danger in such a situation is that highly positive evaluations of PFI projects may lead to a rush in towards PFI without proper provision for adjustments as they come along. On the other hand, in the current scenario in the UAE, it would be hard to implement local construction codes and guidelines religiously. Inappropriate evaluations of PFI, especially in terms of value for money, would lead to hampered progress as PFI project reliability would tend to decrease in the eyes of policy makers and policy implementers in the UAE. In short, it could be surmised that the UAE has a long way to go in order to make PFI a viable reality for its future investment needs in the public sector.

6.1.1.4 Lack of Centralised Economic Measures

The lack of centralised measures in the UAE’s economic structure would tend to affect PFI growth and development negatively. UAE does not have any centralised measure or system under which various emirate governments could coordinate on PFI mechanisms. However, it must be taken to note that the UAE does have a centralised governance structure to coordinate various forms of constructions activities, their applicable standards, guidelines, practices etc. and this structure could be used to coordinate the PFI developments in various emirates. The UAE can replicate Australia’s example as far as the coordination of various PFI structures is concerned. The Australian system of the Infrastructure Minister, the Coordinator General and the

National Minister for Infrastructure[86] can be utilised with ease in the UAE to augment the development and coordination of PFI friendly mechanisms in the UAE. The political situation in the UAE is comparable to that in Australia in certain respects including the fact that various regions tend to operate autonomously to certain extents. However, other significant differences also exist such as the fact that regions in the UAE are not as autonomous as the regions in Australia. Given the various similarities and differences in the Australian and the UAE's political structure, it could be surmised that the Australian PFI arrangement could be brought to the UAE with certain modifications.

6.1.1.5 PFI Models and their Suitability for the UAE

Since UAE's brush with PFI is relatively nascent, UAE needs to examine how different PFI models would tend to operate within the local set of circumstances. There are various PFI model options including (but not limited to) BTO, DBFO etc. While the more liberal PFI markets such as the United Kingdom and Australia support the DBFO model, the more conservative nations such as Japan tend to choose the BTO model. The UAE will need to experiment meticulously in order to decipher if BTO, DBFO or a combined variant would produce the anticipated results for the UAE.

6.1.1.6 Market Confidence

If the UAE chooses to go with PFI in the longer run, it has to provide the investors with an open market unlike the Japanese market that prefers only local investors for small capital venture projects alone. The Japanese implementation of PFI provides a number of things that should not be done to discourage investment, growth and development in PFI. Primarily, the PFI market being targeted by the investors should be open for both local and foreign investors. In addition, the PFI market should provide exposure for both public economic sector projects and public social sector projects simultaneously. Moreover, the PFI exposure of private investors should not be limited to the construction phase alone but instead PFI should take private investors to the service provision stages too. The Japanese example clearly demonstrates that

[86] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

when a public sector intervenes in the PFI sector for tight monitoring and regulation, the eventual result is a stressed and strained PFI sector where the private investor is looking for methods of exodus.

6.1.1.7 Market Structure Changes

Any growth in the current PFI market in the UAE would require certain changes to be carried out in the existing taxation and accounting structures. Similar to Japan, the UAE has developed structures to favour certain investment practices over others. The UAE does not discourage long term equity investments but does promote local investors in preference to foreign investors. With reference to Japan's PFI implementation, it is clear that the UAE would have to provide all private investors with an equal footing to ensure that the PFI sector grows in the longer run. In addition to economic changes and manipulations in the economic structure, the UAE may have to precipitate political changes as well since the inception of PFI will impinge the political and economic interests of the ruling factions.

6.1.2 Implications of Current Political Structures for PFI Growth in the UAE

6.1.2.1 Judicious Political Application

UAE will have to experiment with new provisions and legislation in order to encourage PFI quite similar to Ryrie's Rules in the United Kingdom. Moreover, in the United Kingdom similar sets of rules and guidelines are applied throughout the country but this is not the case in the UAE where different emirates can choose to apply slightly different laws. In order to encourage PFI uniformly across the UAE, it is necessary to include any such legislation or rules in the list of centralised subjects that apply equally all across the UAE. The transition to a PFI friendly framework in the UAE may be helped by the Australian example where one region (Victoria) spearheaded the PFI change. This allowed other regions to emulate the success and to avoid the possible failures from Victoria's example[87]. In addition, UAE will have to remain vigilant so that it does not suffer the same losses that other nations experimenting with PFI

[87] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

suffered such as with the application of Ryrie's second rule. It would be optimal if UAE allowed a well reasoned application of legislation and guidelines that has been concocted after investigating global case studies pertaining to PFI application.

6.1.2.2 ***Political Pressure from the General Public***

The evolution of PFI in the United Kingdom especially in the noughties can be attributed to strong calls for value for money. This move from cost effectiveness in the previous decades to value for money in the noughties can be attributed to political pressure from the public at large. Successive governments have been forced to provide PFI a complete legislative and policy framework in order to encourage fair evaluation of projects such as under *The Green Book* evaluation standards[88]. The situation in UAE is altogether different since there is no elected government and the current government in the UAE need not be accountable to the public at large. The relative absence of political structures, in comparison to the United Kingdom, means that the UAE government would not need to pursue PFI evolution just as aggressively as in the United Kingdom or in Australia. Consequently, the growth and development of PFI in the UAE will be hampered over time since there is no rush from the public sector to develop such an investment scheme through fair evaluation of value for money.

6.1.2.3 ***Legislative Barriers***

The UAE's current legislative framework is comparable to the Australian scenario in the pre 2000 scenario. Legislative barriers in the UAE dissuade wide ranging investment from the private sector. In order to encourage investment in UAE from the private sector for public works, the existing legislative barriers will have to be removed through effective legislation changes. This may prove to be easier for the UAE compared to Australia since there is no elected government and the existing governance structure has the power to implement reforms in the UAE at short notice. On the other hand, the implementation of such policies in the UAE may also prove to be more harmful since there is no elected house to keep a check on the instilled changes. UAE's transition from its current legal framework to a more PFI friendly framework may witness speedy reformation that gets caught up in problems due to a lack of insight. It would

[88] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)

be advisable to exercise caution when implementing PFI friendly reforms in UAE since a rapid deployment may prove more harmful than useful.

6.1.2.4 Political Sensitivities of Local Investors

The UAE presents a class of local investors who must be approached in order to develop business in the UAE. The political sensitivities of these investors will need to be accommodated if PFI is to be implemented in the UAE on a long term basis. When PFI investors are introduced to UAE on an equal footing with local investors, there will be lingering discontent in the local investors who are not used to competition being present. Consequently, this political discontent may provide the current government with large political problems including protests from the local population. The current political volatility in the Middle East in general may provide a background where massive political reformation in the UAE may not be possible. However, as Japan's example demonstrates, in case that major political reformation does not take place, there are little chances to see a growing PFI sector[89]. The UAE may not be able to implement wide ranging political changes given the political consequences the government would have to face. The large amount of political inertia would be enough to discourage development in the PFI sector in the UAE.

6.1.3 Implications of Current Social Structures for PFI Growth and Development

6.1.3.1 Social Attitudes

The attitude of UAE's society needs to change in order to accept foreigners as business owners. PFI mandates that the private sector be provided as much confidence as possible by allowing them ownership of public services so that investment can be encouraged. The current social state in the UAE is harmful to say the least about PFI prospects in the UAE since socially people are not ready to see foreigners as business owners. Consequently, there are chances that unless such attitudes are not changed, there is little chance that investors would tread into the UAE PFI market. In case that some investors do enter the UAE market, their fate would be

[89] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

similar to PFI foreign investors in the Japanese PFI market. Japanese social attitudes have fashioned the need for business ownership from within Japan including PFI projects. The lack of proper sponsorship on the Japanese government's part has led to the PFI market being dominated by small local investors who are unable to take up larger service related PFI projects. Moreover, the current Japanese market for PFI projects is waning given that no major progress is occurring[90]. The UAE PFI market may see similar progression in case that social attitude is not changed towards foreign investors and their role in the formal economy in the UAE. In a globalised world, there can be little place for social attitudes that prohibit foreign entry especially that of foreign investors.

6.2 Survey Results

The survey attached as Appendix A was administered to various government personnel in the Ministry of Finance, Public Works and Foreign Investment and to various project managers working in the construction sector in order to discern their concerns for PFI growth and development in the UAE. The results of the survey are discussed below in detail to discern obstacles to PFI growth and development along with various prospects for such growth and development.

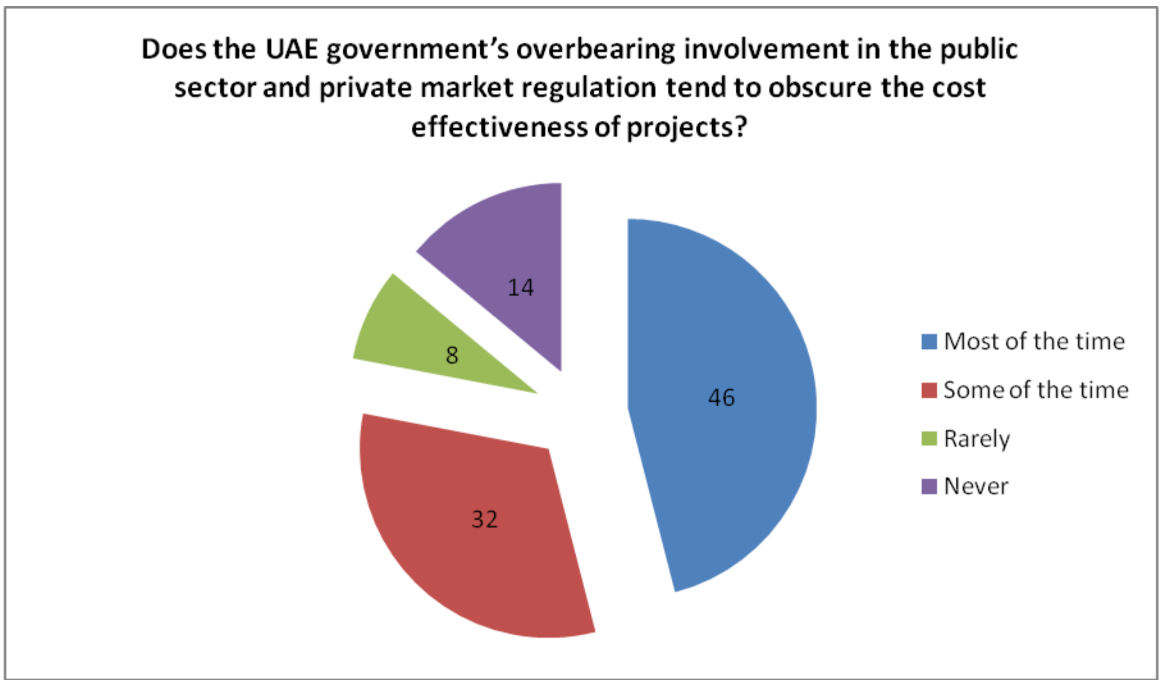
The results of the survey revealed that the majority of respondents blamed UAE's nascent efforts at PFI for stunted PFI growth. Almost 60% of all respondents responded affirmatively when asked if UAE's limited exposure (in terms of time) was to blame for stunted PFI growth. In contrast, some 30% of all respondents believed that PFI's stunted growth in UAE's case was not attributable to lack of exposure (in terms of time). Additionally, some 10% of all respondents failed to see any connection between the time that PFI had been implemented in the UAE and the stunted growth of PFI in the UAE.

The survey also revealed that most respondents saw the UAE capable enough to develop indigenous solutions for PFI mechanisms that the rest of the region could copy. Some 80% of all respondents believed that the UAE could develop PFI on its own without any help from the MENA region such that the solution developed by the UAE would be emulated region wide. In

[90] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

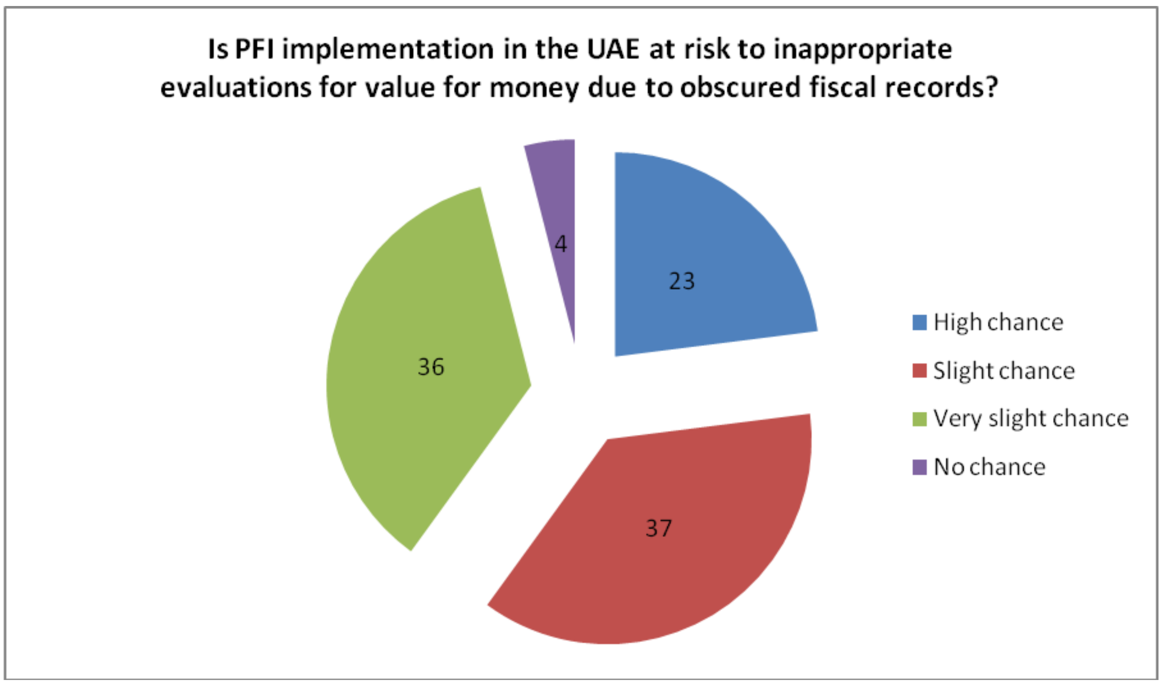
contrast, only 20% of the respondents saw the need for wider regional cooperation if the UAE was to develop a PFI mechanism.

In terms of obstacles to PFI, a significant number of respondents saw the involvement of the UAE government in the public sector and the private markets as leading to obscured cost effectiveness of various projects. The respondent output on this question is shown in the pie diagram below. Some 46% of the respondents agreed that the government's involvement caused cost effectiveness to be obscured most of the time while some 32% of all respondents believed that it occurred only some of the time. Only 8% of the overall respondents saw the UAE government's involvement as being rare while 14% did not believe that the government interfered at all. The results are shown graphically in the diagram below. In terms of the results, it is clear that most people see the government's interference in the public sector and the private markets as causing problems for cost effectiveness. The respondents who believed that some kind of a problem exists add up to 86% while only 14% of all respondents believed that the government never interfered at all.



In result to another question, most respondents believed that the current global economic turndown would be enough impetus to force the UAE to adopt PFI as a viable solution. Some 56% of all respondents saw the current global economic turndown and the resulting inflation enough to force the UAE government to pursue PFI more aggressively. In contrast, only 13% of all respondents saw no such need while some 31% of all respondents believed that such circumstances would maybe force the UAE government to pursue PFI more aggressively.

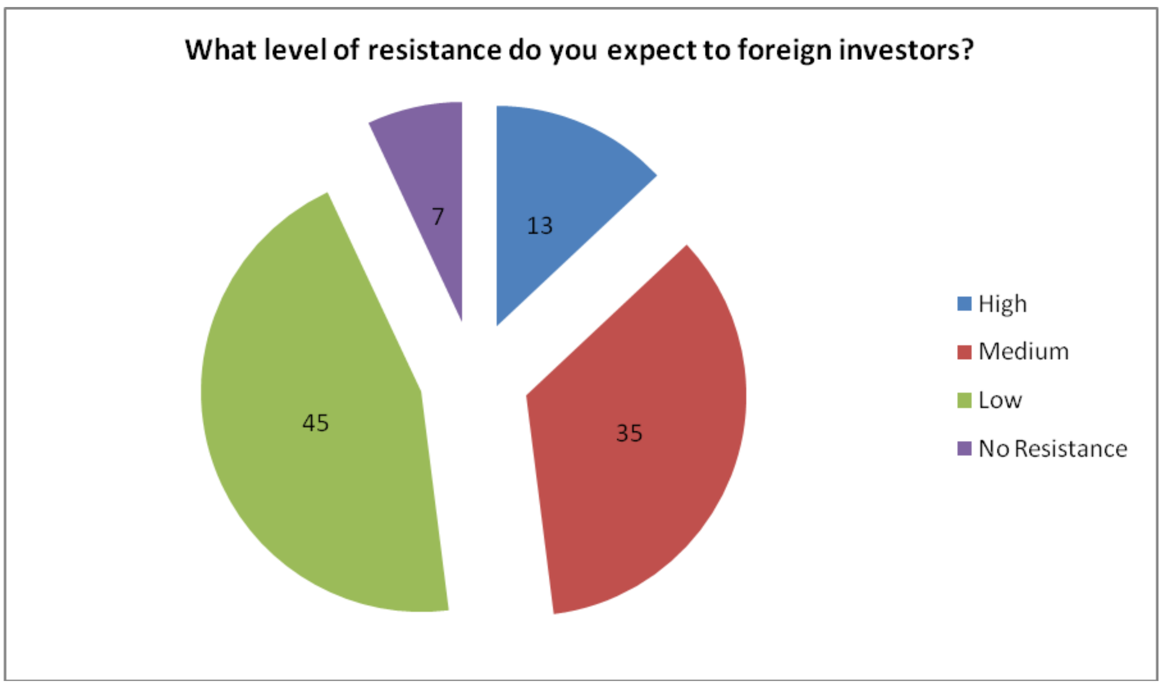
The involvement of the UAE government in market regulation was tested through another question to gauge consistency. The respondent output on this question is shown in the pie diagram below. The results showed that most people saw PFI implementation in the UAE at risk to inappropriate evaluations for value for money due to obscured fiscal records. Some 23% of all respondents believed that there was a high chance for inappropriate evaluations to take place while some 37% of all respondents saw a slight chance. On the other hand, some 36% of all respondents saw only a very slight possibility for inappropriate evaluations while some 4% of all respondents saw no chance. Overall, it could be said that some 96% of all respondents saw PFI at risk due to inappropriate evaluations while some 4% did not perceive such risk.



In response to the strength of the UAE union in implementing PFI, some 17% of all respondents saw the union as ineffective while an overwhelming 83% saw the union as strong enough to implement PFI. It could be surmised that there is an overwhelming confidence in the strength of the UAE's political union and its strength in implementing various policy changes. On the other hand, when questioned about the restrictions on business ownership in the UAE and the resulting market entry barriers for large foreign investors, most respondents (92%) saw entry barriers while only 8% did not see any entry barriers. Similarly, when asked if the foreign investors in question would form the bulk of the PFI sector in the UAE, most respondents saw only a minimal role for foreign investors (28%). Most respondents in the survey (72%) were confident that local investors would be enough to create the bulwark required to support PFI operations in the UAE. Additionally, when questioned if the ruling classes and their economic interest would be hurt by PFI implementation, most respondents replied in affirmative (56%) while others (44%) replied negatively). However, the results were unable to provide substantial support for either point of view since there was no clear majority in either standpoint.

On the other hand, when questioned if the UAE's current legislative framework was robust enough to support legislative changes required to implement PFI, there was no clear response. Around half of the respondents (47%) saw the current legislative framework as being robust enough while the other half (53%) saw the current legislative framework as not being robust enough. In stark contrast, when the respondents were questioned if the UAE government was performing well enough in the current circumstances, a clear majority though that the performance was good enough. Only 22% of the respondents saw the UAE government as performing ineffectively in the current set of circumstances while an overwhelming 78% were satisfied with the government's performance in the current set of circumstances. Given the government's perceived strong performance, the respondents were asked if such strong performance did not call for a strong value for money in the UAE. The results demonstrated that most people (83%) believed that the current economic arrangement did not call for a strong value for money in the UAE while only a small proportion of respondents (17%) tended to disagree.

Most respondents (63%) saw oil revenues as being enough to support future growth in the UAE while only a small proportion (37%) tended to disagree. On the other hand, when asked about the role of the FNC in political decision making within the current political arrangement, most respondents (76%) saw the FNC's current role as allowing expedient legislative change. In contrast, 24% of the respondents saw the FNC's role causing damage to the credibility of the legislative change process. When respondents were presented with the option of allowing foreign investment and its allied legal and judicial aspects to be cast as a federal subject for all emirates to follow, only a small proportion of respondents (29%) agreed to the idea. In contrast, an overwhelming majority (71%) of all respondents were of the view that making foreign investment and its allied legal and judicial aspects a federal subject would only produce unwanted political tensions in the UAE union. Most respondents (85%) also wanted to see legislative changes towards PFI implemented gradually rather than immediately. When respondents were asked if local investors would allow foreign investors to enter the market, the response remained ambivalent. The respondent output on this question is shown in the pie diagram below. Some 43% of the respondents saw local investors allowing foreign investors to enter the market while the remaining 57% saw local investors as blocking any such moves. Similarly, when asked what level of resistance the local investors would provide the foreign investors, some respondents (13%) believed that a high level of resistance would be offered. In contrast, a significant proportion of respondents (35%) believed that a medium level of resistance would be offered while around half (46%) of all respondents believed that a low level of resistance would be offered. In contrast, only 7% of all respondents believed that local investors would offer no resistance to the entry of foreign investors into the UAE market. Therefore, the overwhelming sentiment from the survey reveals that local investors would resist moves to allow foreign investors to enter the local market, especially as business owners and operators.



6.3 Discussion

Most respondents saw the UAE as capable enough to develop an indigenous PFI solution to suit its own needs and to provide as a model for the rest of the region to emulate. Interference of the central government has to be controlled in order to deal with current cost effectiveness problems. In case that proper cost effectiveness cannot be determined, there are chances that initial PFI implementation may overestimate or underestimate the viability of such options for solution provision in the public sector. Consequently, even if PFI projects would be successful on ground, they would still seem like failures on paper. In the longer run, such an arrangement would tend to underscore PFI implementation more than being able to augment it.

Survey results show that most respondents believe that the UAE government would be forced to pursue PFI more aggressively in order to deal with the current global economic turndown and the resulting inflation. It could be said that people in the UAE are cognisant of the fact that the UAE government is hard pressed for development in the longer run under current circumstances even though most people are not ready yet to allow foreign investors as business owners in the UAE.

It must also be noted that survey results overwhelmingly proved that PFI implementation in the UAE was at risk due to inappropriate evaluations. It must be kept in mind that PFI implementation stands at greatest risk, especially in the longer run, due to inappropriate evaluations because of the reduced credibility of the overall process. Given the fact that PFI projects have been more successful on ground but have still come under criticism due to inappropriate evaluations around the world, it is imperative that PFI evaluation mechanisms be augmented in the UAE. Even though PFI implementation has provided projects with lower cost and schedule variance but even so PFI has come under critique for being ineffective. There is a high chance for this to occur in the current circumstances in the UAE.

Most people trust the strength of the UAE’s political union in being able to implement system wide policy changes such as the PFI framework. However, it must also be noted that there are political stumbling blocks that are out to prevent PFI implementation. For example, the survey reveals that the majority of people see business ownership in the UAE for foreign investors as being problematic for PFI development. In contrast, most people also tend to believe that foreign investment is not really required to support PFI development in the UAE since local investors would be able to support the push towards PFI development in the UAE. With the current set of results, it becomes clear that people place confidence in the political strength of the UAE’s union to allow system wide policy changes without realising that business ownership rules must be changed and that unless this is done, there are little chances for PFI growth in the UAE. In comparison to the Japanese example, it becomes clear that local investors, no matter how large, cannot be expected to take onto PFI growth and development in the longer run[91]. If the UAE wants to implement PFI in a system wide manner, there is ample need to alter current business ownership rules in order to allow foreign investment to enter the market.

Another major aspect of PFI implementation, especially in terms of PFI evolution, is a strong call for value for money. There are already ample PPP arrangements in the UAE but there are only a few arrangements that can be classed as PFIs. It must be taken into consideration that the United Kingdom only moved towards PFI from more fluid PPP arrangements once there were overwhelming calls for value for money. Such a set of circumstances only came into being because the government was representative and the people on ground were involved in the governance process. In contrast, the UAE exhibits an altogether different situation since the common man has little to do with governance. Moreover, in terms of the United Kingdom example, economic strain forced the government to commit in the direction of PFI. However, the survey results reveal that the people in the UAE do not see their economic circumstances strained enough for the government to rush into PFI arrangements. Consequently, it could be surmised that PFI implementation in the UAE would take some time as there are no immediate catalysing factors supporting the evolution from PPP to purely PFI arrangements.

The role of the FNC in political decision making was also clarified in terms of the survey as most respondents saw the FNC's role as a catalysing agent for legislative changes. Only a small proportion of people saw the FNC's role as causing damage to the credibility of the legislative change process. This in turn means that most people are satisfied with the political arrangements in the UAE with respect to the executive and the legislative. Hence, it could not be expected that there could be system wide political changes that would either favour PFI implementation or stall PFI implementation in the longer run. This idea was also confirmed when respondents were asked about allowing foreign investment and its allied legal and judicial aspects to be cast as a federal subject. Most respondents disagreed to such an idea and saw it as inviting unwanted political tension for the union. This indicates that neither the people in the UAE, nor the government is looking at system wide or otherwise pervasive changes in the

[91] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

political structures. Consequently, the road to PFI in the UAE seems to be obstructed by a number of political obstacles that seem hard to remove.

It has also become clear that local investors could be expected to resist the entry of foreign investors into the local market. This could be carried out in a number of different ways that would require political support. Given the current set of circumstances, it is clear that foreign investor’s entry into UAE’s local market is fraught with various obstacles. However, it needs to be kept in mind that as long as local investors do not allow foreign investors to enter the market, the prospects for PFI growth and development are bleak.

7 Chapter Seven – Conclusion and Recommendations

7.1 Conclusion

PFI implementation in the UAE has been slowed down by a number of challenges including economic, political and social challenges. It has to be realised that implementing PFI in the UAE is challenging but considering the current global and local economic conditions, the eventual implementation of PFI in the UAE cannot be denied. In order to deal with PFI implementation in the UAE, political will has to be garnered to allow foreign investors to enter the UAE market as equals of local investors. Unless foreign capital is not allowed to move into the local market, there would be no point in trying to run after PFI since it would only provide a stalemated situation such as in Japan. The economic changes including market reformation and structural changes in the economy for PFI implementation will only be possible if proper political and social reformation is allowed to take place. It would be advisable to pursue gradual changes especially on the political front to create the required momentum to overtake the current inertia holding back PFI growth and development in the UAE.

Currently the UAE faces myriad challenges on the political and social fronts in PFI implementation that in turn tends to affect the economic structures required to support PFI implementation. In order to move forward, the UAE has to make its people realise that PFI implementation is inevitable and the sooner it is put in place, the better the results would be. Additionally, the PFI implementation effort should be augmented through the use of political will creation especially from the more affluent groups in the UAE. A complete social and political transformation allowing the entry of foreign investors into the market is the real guarantee that economic reformation will occur to support PFI implementation in the UAE in the longer run.

7.2 Recommendations

Broadly speaking, UAE's brush with PFI is wrought with multi-dimensional barriers that encompass economic, political and social dimensions. PFI's greatest barriers lie in terms of the economic structures available in the UAE but it needs to be kept in mind that the current economic structures are a result of the peculiar political and social conditions that make up the UAE.

One of the first things to keep in mind is that the UAE's experience with PFI is a nascent one. Moreover, the UAE's drive towards PFI is not supported by other regional nations. Therefore, it would be hard to expect UAE to overcome tremendous challenges immediately to implement PFI as a solution to upcoming economic challenges. It would be reasonable to expect that the UAE would be able to implement PFI over time but such a development could stretch into decades. In order to take PFI into the broader economic perspective, the UAE government needs to perform cost effectiveness studies which can only take place with the right kind of data collection. It would be pertinent to start with PFI in the UAE with something similar to Ryrie's Rules[92] in order to take PFI onto the right track.

Another major requirement for PFI implementation is determining the right value for money in various projects around the UAE. The value for money debate needs to be settled to determine which infrastructure and services ought to be included in the PFI framework. Local construction codes and guidelines ought to be enforced stricter than at present in order to determine the real value for money provided by the PFI mechanism. On another note, it would be highly beneficial if PFI can be implanted in the UAE uniformly within the seven emirates using centralised measures. The UAE could experiment with PFI in the more progressive emirates such as Dubai and Abu Dhabi in order to find centralised solutions for the rest of the UAE. This move would be comparable to the approach used by Australia to expand the Partnerships Victoria programme to a fully fledged PFI mechanism. Given that this approach has produced results in the past, it is advisable to take this approach in the case of UAE's move towards PFI.

In addition, the UAE would have to experiment with various models under existing PFI mechanism to determine what models would tend to suit the UAE's peculiar socio political and economic circumstances. The major options available to the UAE would be the BTO and the DBFO models in use around the world. Given the current scenario, it would seem that a mixture of the BTO and the DBFO models would be best implemented for PFI in the UAE. However, it would need to be seen as to which projects would develop favourably under BTO and which would develop favourably under DBFO.

[92] Abdelhalim Boussabaine, *Cost Planning of PFI and PPP Building Projects* (London: Routledge 2006)

One of the more contentious issues in terms of PFI implementation in the UAE remains investor confidence. There have been instances where the UAE government has intervened in PPPs to convert them into purely government funded and supervised projects[93]. This form of measure has shaken investor confidence such that large investors may shirk from entering the UAE PFI sector for a long time. The Japanese example demonstrates that as long as market confidence is not provided to the prospective international investor, there is little chance that the PFI sector can take off[94]. The UAE needs to make clear policies in order to develop market confidence for investors especially the larger international investors. The real road to growth in terms of PFI for the UAE lies in allowing foreign investors to operate freely in the UAE so that investor confidence allows catalysed development of PFI. The typical UAE approach to favour local investors, rather to promote local investors over foreign investors would not allow a judicious development of PFI. The UAE has to learn to allow foreign investors greater freedom and privilege in case the UAE wants to emulate PFI examples from Europe.

Another area requiring immediate attention for PFI growth in the UAE is the political structure. The current political arrangement in the UAE tends to favour the local investor, especially the larger local investors who are connected to the ruling classes. The political pressure exerted by such investors in particular and from ordinary UAE citizens in general have meant that business ownership in the UAE has remained confined to local people alone. In order to encourage PFI growth in the UAE, it is imperative that such entry barriers be removed. However, this is easier said than done. The best method of achieving a fair playing field for local as well as foreign investors would be to introduce gradual reformation in the business ownership rules. There is a move to amend the Federal Company Law but it has been unable to take off for a number of years given the ambitious nature of the document. The large number of reforms planned under the subject change has failed to win the approval of the involved political actors. The optimal method would be to introduce gradual reform by amending the requisite laws sequentially as required.

[93] Tim Burbury, *Infrastructure and Project Finance* (Financier Worldwide 2012)
[94] JETRO, *Public Private Partnerships in Australia and Japan: Facilitating Private Sector Participation* (JETRO 2010)

7.3 Future Research Areas

PFI implementation in the UAE can only move forward once suitable models for PFI implementation are decided upon. UAE's PFI implementation could take the path of BTO, DBFO or a combination of both as per individual project needs. The current research has provided for various factors that intertwine the economic, political and social exigencies that need to be considered to implement PFI in the UAE. However, the model required to deal with PFI implementation in the UAE has not been considered. Future research in this area should consider the various models for PFI implementation around the world to decipher what model or combination of models would be most suited to the UAE situation.

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9 Appendix 'A' – Survey

1. Do you believe that UAE's limited exposure (in terms of time) with PFI is to blame for stunted PFI growth?
    a. Yes
    b. No
    c. Time has nothing to do with PFI growth
2. Can the UAE develop PFI on its own in the MENA region to allow its neighbours to copy such a solution or does the UAE need the support of its neighbours to develop PFI?
    a. The UAE can develop independently;
    b. The UAE needs regional support
3. Does the UAE government's overbearing involvement in the public sector and private market regulation tend to obscure the cost effectiveness of projects?
    a. Most of the time
    b. Some of the time
    c. Rarely
    d. Never
4. Is the current global economic turndown and the resulting inflation enough to force the UAE government to pursue PFI more aggressively?
    a. Yes
    b. No
    c. Maybe
5. Is PFI implementation in the UAE at risk to inappropriate evaluations for value for money due to obscured fiscal records?
    a. There is a high chance
    b. There is a slight chance
    c. There is a very slight possibility
    d. There is no such chance
6. Do you see the UAE's union as weak and ineffective in trying to implement PFI mechanisms in different emirates?
    a. Yes
    b. No
7. Do you believe that the current restrictions on business ownership and operation in the UAE tend to prohibit large investors from entering the market?
    a. Yes
    b. No
8. If you answered yes to the previous question, do you see such large investors as forming the bulk for UAE's future PFI sector?
    a. Yes
    b. No

9. Will the implementation of the PFI mechanism tend to affect the economic interests of the ruling classes?
    a. Yes
    b. No
10. Do you see the current legislative framework in the UAE as unable to support legislative changes required to implement PFI?
    a. Yes
    b. No
11. Do you see the UAE government performing well enough in the current circumstances?
    a. Yes
    b. No
12. If you answered yes to the previous question, do you believe that the current economic arrangement does not call for a strong value for money in the UAE?
    a. Yes
    b. No
13. Do you see oil revenues as being enough in the future to sustain UAE's economic growth at the current pace?
    a. Yes
    b. No
14. Does the limited participation of the Federal National Council in legislative decision making allow for expedient legislative changes or does it corrode the credibility of such change?
    a. It allows for expedient legislative change
    b. It damages the credibility of legislative change
15. Should foreign investment and its allied legal and judicial aspects be bundled as a federal subject and implemented equally in the seven emirates under the constitution?
    a. It should be cast as a federal subject
    b. It would produce unwanted political tension
16. Should legislative changes for PFI implementation be gradual or immediate?
    a. Gradual
    b. Immediate
17. Will local investors and business owners allow foreign business owners to enter the local market at all?
    a. Yes
    b. No
18. If you answered yes to the previous question, what level of resistance do you expect?
    a. High
    b. Medium
    c. Low
    d. No resistance