Investment in infrastructure: the way of Latin America towards development

The Uruguayan case

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I. Introduction

The economies of Latin America, including Uruguay, are going through a major process of growth, for which they are not fully prepared.

Focusing on Uruguay's economy, after the deep depression experienced in 2002, it has been growing by leaps and bounds. This growth, which was not expected by economists and therefore not planned by the government, had to overcome several obstacles in order to continue to develop.

One of the main obstacles is the lack of infrastructure for the major foreign projects which have chosen Uruguay as their location. Indeed, to sustain the country's current economic growth, it is essential to have adequate infrastructure. This has a direct impact on productivity and international competitiveness, which in turn leads to higher social welfare and a better quality of life.

The gaps in infrastructure have been expressly recognized by investors, economists, government officials and international organizations. Those tasked with leading the country are working to find possible ways to allow the Uruguayan economy to continue growing despite the lack of adequate infrastructure.

The path is marked. According to studies from different public-sector agencies, as supplemented by economic analyses provided from the private sector,[1] eliminating those gaps would require investments that can be estimated at 5 billion dollars. Amounts like these are extremely relevant given the size of Uruguay and its economy, and finding such investments will probably make a significant difference.

The challenge is then to find the appropriate regulations to allow for such investments to be made and for business opportunities in Uruguay to be desirable for both foreign and domestic capital.

In the light of the above, a regulatory framework was created with the purpose of ensuring the sustainability of projects through Public-Private Participation (PPP).

[1] Information provided by CPA/FERRERE Consultants – Economist Alfonso Capurro

In this connection, this paper attempts to analyze PPPs as one of the remedies recently proposed in Uruguay on this subject. We will begin with a brief glimpse of the country's main features, in a general and institutional way. We will analyze the infrastructure needs arising in Uruguayan society and how these needs are read throughout the world. Finally, we will introduce the recent legislation on Public-Private Participation, discuss its background, explain the proposed scheme, and attempt to draw conclusions concerning the aim of this new law to solve problems in infrastructure.

II. Uruguay. A snapshot.[2]

In order to understand the infrastructure needs in countries like Uruguay, it is important to understand the country's characteristics. The following are some illustrative data to be taken into account.

The population of Uruguay is currently estimated at 3.4 million people; some 1.3 million people live in Montevideo, the capital city, as well as in large cities and neighboring areas, while the rest of the Uruguayan population is distributed in smaller cities and rural areas. Uruguay's population growth is 0.6% per annum, one of the lowest in Latin America, similar to that of most developed countries. The economically active population totals 1.5 million people.

Traditionally, Uruguay has sustained a strong economy mainly based on agriculture and primary-sector exports, but with a rapidly growing predominance of the services sector as shown by a thriving tourism industry and development of offshore banking and other services. Leading economic sectors include meat processing, agribusiness, wood, wool, leather production and apparel, textiles, and chemicals, together with a swiftly developing software industry.

Uruguay's strategic location in Latin America as one of the main regional ports, its political stability and democratic tradition, its high educational and living standards, its rapidly growing economy and a favorable, investor-friendly approach to business create an ideal climate for the channeling of foreign investment.

[2] Information provided by CPA/FERRERE Consultants – Economist Alfonso Capurro, and obtained from Report of the WORLD ECONOMIC FORUM: The Global Competitiveness Report 2011–2012.

In the last decade the Uruguayan economy has experienced one of the most dynamic periods in its history, with an average annual growth rate of 6.3% between 2004 and 2010. Growth was partly driven by a significant expansion of the primary sectors, particularly agriculture and forestry, which has necessarily generated increasing pressure on the country's infrastructure. The agricultural area grew five-fold in the last decade, while the maturity of the country's forest mass has led to the installation of industrial complexes such as wood veneer and wood pulp plants.

This growth has allowed the country to regain macroeconomic stability, climbing from 107th to 59th place according to the World Economic Forum (WEF). Economic growth has also been led by private consumer spending. This scenario has permitted a reduction of the government deficit and the overall level of public debt in the last years.

WEF says that the country leverages its traditional competitive strengths because of its transparent and well-functioning public institutions (the corruption index is low). This situation has put Uruguay in 35th position worldwide. Also, Uruguay shows very high rates of education enrollment (16th place for primary education and 25th for tertiary education) in comparison with other countries in the region.

However, despite this progress, inflationary pressures and the reduction of the national savings rate suggest an overheating of the economy, which can bring about significant macroeconomic distress if not properly tackled. Moreover, as Uruguay keeps growing and moves steadily towards a higher stage of development, policies to increase domestic competition that would provide incentives for higher business-sector investment in research and development and innovation capacity will become increasingly important.

III. Infrastructure. Importance and needs in Uruguay

As recognized by specialists, extensive, high-quality infrastructure is an essential driver of competitiveness, impacting significantly on economic growth and reducing income inequalities and poverty in a variety of ways for any country.[3]

[3] World Economic Forum, *"Benchmarking National Attractiveness for Private Investment in Latin American Infrastructure,"* page 4.

A well-developed transport and communications infrastructure network is a precondition for making markets work efficiently. It will help with the local internal market, as well as the international market, by constructing a framework that will enhance export growth.

a. What is infrastructure and why is everyone talking about it?

The term infrastructure is commonly used to refer to *"all physical assets, equipment and facilities to provide essential services for the life of communities in a given time."*[4]

These essential services can be of various kinds. On the one hand, there are those which are mostly focused on economic development in a given community at a given time, such as transport services (roads, railways, ports and airports, etc.), telecommunications and power grids. On the other hand, there are those essential services which have a social profile. The latter are those recognized as "social services" and refer to health, education, security, etc.

This distinction allows us to talk about two types of infrastructure. The type that will meet the needs of the first group is called economic infrastructure. The type necessary to build a framework to ensure compliance with social services is called social infrastructure.[5]

Providing our societies with sufficient quality infrastructure is a political-economic decision that requires immediate response from governments. Taking the decision to cover existing infrastructure needs will set the scenario for developing economic activity as a whole, and will be, as mentioned above, an incentive that will make our countries attractive for investment.

b. Uruguayan situation in terms of infrastructure

As mentioned at the outset of this paper, Uruguay's economy is going through one of the times of greatest growth in its history. Prior to 2004 (excluding the severe depression experienced in 2002) growth averaged no more than 2% annually. From 2004 to date the average annual growth rate has been 6.3%.

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[4] Echeverría Petit, José Luis, "*En el foco de la discusión nacional: infraestructura y participación público privada,*" Tribuna del Abogado, nº 173 (jun./jul. 2011), pg.5.
[5] Echeverría Petit, José Luis, Op. cit., pg.5.

Factors that have contributed to this growth are the expansion of the primary sectors, particularly agriculture and forestry. Logistics and transportation needs for the development of these areas increase pressure on infrastructure networks in the country.

b.1 Economic infrastructure. In recent years the Uruguayan government has offered opportunities for private investment in infrastructure in the country: road networks, railways, port facilities and airport system. Also, guidelines were established to encourage investment in energy. Here we review the different economic infrastructure scenarios that require attention in this country.

b.1.1 Roads. "*Roads are at the heart of how we live today. They are part and parcel of our individual lives and are fundamental to facilitating and encouraging economic growth across regions, countries and continents."*[6]

Uruguay has an infrastructure in terms of roads that allows access to its entire territory. However, the pressure to meet the infrastructure needs associated with the road network is enormous.

In 2010 the national road network consisted of 8,782 kilometers. 50% were international highways and primary network, while the so-called tertiary network represented 10%.[7]

Regarding the quality of this network, 3% of the roadways are of concrete, and 36% are made of asphalt. Materials with lower resistance to traffic and weathering, such as bituminous and gravel, make up 49% and 12% of the network, respectively.

In recent years, road investment focused on new works, reducing the resources available for maintenance of the network. Maintenance has kept step with increases in construction costs, which ultimately has resulted in less investment in this connection.

Additionally, investment has grown less than traffic, leading to a reduction in the life of the road network and its further deterioration.

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[6] DARE, JOSS, "Roads", Public-Private Partnerships, page 11.
[7] Additionally, the road network has approximately 50,000 km of rural roads and departmental network.

In effect, the significant volume of traffic on Uruguayan roads in recent years[8] has meant that the state of our roads is not optimal. In this regard, the government has sought investments to improve conservation status of the roads, demolishing bridges with load restrictions and building new ones, reducing the sections that cross population centers, improving the quality of materials used, etc.[9]

The Uruguayan Construction Chamber estimates that Uruguay has an infrastructure deficit of approximately 1,150 million dollars. However, with each day that goes by without the required investment being made, new skills requirements are generated and gaps in road infrastructure continue to grow. In addition, as mentioned above, it should be noted that investment in infrastructure must be projected to the future and that beyond the new works that may be required a large investment is needed to maintain the existing ones. In this regard, studies estimate a budget allocation of 400 million dollars annually is needed to keep up infrastructure.

Regarding this scenario, our Government offered some projects to private investors and the first project to be done through the Public-Private system will be the rehabilitation of routes 21 and 24. Initially, the idea was that earlier this year the works would already be on their way, but the government now aims to call for bids in three months.

The investment that will be required by this project is in the area of 100 million dollars. The mechanism defined for the awardee to receive income for project execution will be divided into the toll paid by users and the transfers made by the Government depending on use of the highway (shadow toll). The percentages of the two types of income are yet to be set.

The term for operating the highway will be twenty years and the private party will be required during that time to handle maintenance of the roadway and ditches, cleaning of shoulders, signage, lighting, and motorist assistance.

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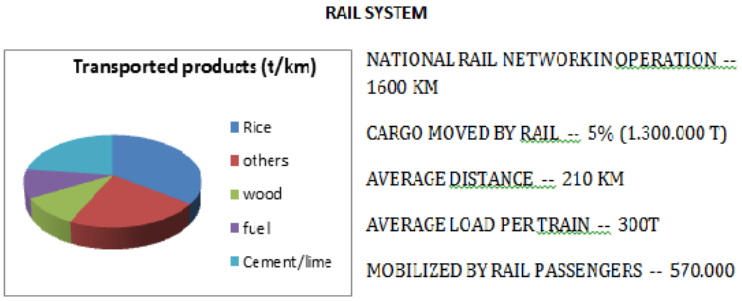
[8] Specially produced by the growth of the agribusiness, the mining and the forestry.
[9] CAF Report on *"Linking private capital in the development of transport infrastructure projects and energy in the Oriental Republic of Uruguay*", Volume I and II

b.1.2 Railways. The railway system was heavily depressed in Uruguay. In recent years, a series of improvements and maintenance work has been done; and work has begun on the construction, rehabilitation and maintenance of railway infrastructure.



Source: MTOP presentation

The investment estimated for the construction of the railway branches that the Government considers necessary to meet the material needs of railway infrastructure is estimated at approximately 260 million dollars. This amount does not include the investment required for the purchase of locomotives, railway cars, and other necessary machinery.

b.1.3 Ports. As they are strategically located between the major consumer centers in Latin America, Uruguayan ports are very attractive doing business in this part of the word.

The main commercial port in Uruguay is Montevideo, the country's capital. Annually, this port moves approximately 10 million tons of cargo, 500,000 passengers, and 100 cruise ships. The port handles containers, general cargo, bulk, logistics depots, fishing as well as passenger and cruise ships. There are also other major ports in Uruguay, such as Nueva Palmira in Colonia.

As for investment in infrastructure, the government is looking for projects to improve port equipment (purchase of dredgers, purchase of boats, cranes, etc.) as well as projects to build new additional ports. The most important project nowadays is the project involving the construction of a deep-water port in Rocha (which is very important for the investments projected in sectors such as mining and forestry).

Additionally, large sums of money must be allocated in order to carry out dredging works for the purpose of ensuring the desired artificial depth of rivers adjacent to the active ports, thus ensuring the movement of boats in ideal conditions.

Finally, we cannot fail to mention the projects that have been considered for the construction of an additional container terminal. This is one of the largest infrastructure projects under study in recent years. The port terminal is currently operating at 100% of its capacity, and there are different projects at the stage of conducting feasibility studies on the construction of a second container terminal and expansion of the existing one.

Source: MTOP presentation

b.1.4 Airports. As for investments in infrastructure to carry out works at the airports, we note that efforts are being made to rehabilitate some airports that have not been used for a long time and which status is precarious (Colonia, Salto and Rivera). The purpose is to serve the region and enhance resorts across the country.

b.1.5 Energy.[10] According to WEF, Uruguay currently ranks 35th in the world for energy-supply infrastructure.

Service coverage is greater than the average public service providers of electricity. Apart from continuing to extend its distribution networks, the government is providing the rural population with modern energy services: solar panels in places where conventional grid extensions are not economically viable. However, there is still much to be done in the field of energy, especially considering the crisis in the region.

[10] Data taken from World Bank publication: "URUGUAY INFORME DE POLÍTICA DE DESARROLLO (DPR) - *Eficiencia en Infraestructura Productiva y Provisión de Servicios Sectores de Transporte y Electricidad"* and from the report *"Oportunidades de inversión en Uruguay- Energías Renovables"* prepared by Uruguay XXI.

Indeed, for the coming decade an increase of nearly 40% in the demand of electricity is expected in Latin America. This growth will not only have implications for the electrical industry, but will affect society's basic needs.

Uruguay has developed most of the large-sized hydropower capacity available in its territory. The thermal plants which are available are low yield, due to their age or because they were designed for small energy production.

To minimize the use of backup power, Uruguay has supplemented its hydroelectric energy production with hydroelectric energy imports, especially from Argentina. However, the energy crisis suffered by Argentina is forcing Uruguay to investigate new alternatives which welcome investments in this sector.

Indeed, the strong growth of energy demand due to high GDP growth rates, the lack of native fossil fuel resources and the limited room to incorporate hydroelectric generation led the Government to develop policies to raise non-traditional renewable native energy sources.

Uruguay has good solar radiation and large wind and biomass resources which are useful in the development of agriculture, livestock and forestry.

Uruguay is seeking greater diversification of its energy matrix, incorporating native resources, especially renewable ones, expecting the development of private participation in electric power generation using renewable energy.

The objective of this policy is the satisfaction of all national energy needs, at appropriate costs for all social sectors, by bringing competitiveness to the country, promoting healthy habits of energy consumption, ensuring the country's energy independence within a framework of regional integration through sustainable policies from both economic and environmental points of view, using energy policy as a tool to develop production capacities and to promote social integration.

Based on this, greater diversification of the energy matrix is expected, including native unconventional sources and increasing private participation for native generators. The

goals set for 2015 include incorporation of 500 MW from wind power, 200 MW from biomass and 50 MW from small sources of hydro energy.

b.1.6 Telecommunications.[11] Access to networks (information, entertainment, social and personal communication) is now a necessary condition for integration into modern society. In a regional perspective, Uruguay is in a relatively good position in the telecommunications sector.

This sector represents about 7% of GDP and continues to grow. It is seen as strategic for development, both because of its impact on the economy and attracting investment, and its importance for the integration and equity in a knowledge society.

There is good phone service coverage (about 1,000,000 fixed telephony services and over 4,000,000 cell phone services according to URSEC[12]).

In broadband, we have acceptable coverage: 350,000 fixed broadband services, and tens of thousands of mobile Internet services. However, the quality of broadband is not good: the average speed is lower than in other countries in the region.

Paid TV is present in major cities, with different technologies (digital and analog cable, digital TV and analog wireless, satellite TV). It is estimated that around 470,000 services have been installed, a little less than 50% of them in Montevideo.

From the point of view of economic dynamics this is an imperfectly competitive market, with some monopolies and oligopolies: the "incumbent operator" (ANTEL) exercises a monopoly in some areas (fixed telephony and fixed broadband). Two large multinational enterprises challenge it (only in cellular and mobile Internet), which aggressively captured a significant share of the market. Nowadays, market share between these companies is relatively balanced at approximately 40%, 40% and 20% (Ancel, Movistar and Claro, respectively).

[11] Data taken from The Telecommunication Chamber of Uruguay - Telecomunicaciones de Uruguay - http://www.telecomunicaciones.org.uy
[12] Regulatory Unit of Communication Services (Unidad Reguladora de Servicios de Comunicación - URSEC)

Subscriber TV operators constitute another oligopoly, covering particular geographic areas, and there is also a contender for national satellite (DirectTV). Permissions for other satellite TV operators have been denied by the government (TELMEX in 2008). Cable operators want to expand into other services such as broadband cable modem, but those permissions have not yet been given by the government.

Regarding investment, there is a project for working on social inclusion and universal access, convergence of networks and the confluence of TV with Internet, bringing in high-speed Internet mobile networks (LTE services "long term evolution" and 4G), fixed access FTTH (optical fiber direct to home) that enable a new generation of massive scope contents.

The required investments are significant. Some countries have faced them as public works, without expecting a quick payback. Others have chosen to leave them to private hands, with public regulation.

However, Uruguay has excluded telecommunications from the field of PPP, and has thus relegated it to the public sector.

b.2 Social infrastructure. Social infrastructure, as mentioned, gives support so that essential services which have a social profile can be enjoyed by most of the population.

b.2.1 Prison system.[13] The Uruguayan prison system is in crisis. The Uruguayan government faces many challenges in its attempt to reform the prison system. These include, among others, the problem of finding an answer to decayed conditions and serious levels of overcrowding in some institutions.

At present, the system capacity can be estimated at 7,500 places, but we have a population of convicts which is about 10,000.[14]

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[13] Information provided by the Parliamentary Commissioner for the Prison System, Dr. Alvaro Garcé

[14] Place: the place provided for the accommodation of a person under acceptable conditions. Internationally there is no set area or capacity. The estimate of number of required places was made by the Parliamentary Commissioner for the Prison System in 2010, according to UN standards.

The principal detention center is the Comcar which houses 3276 people, even though it has a capacity of 1,600 places. The second most important detention center is the Libertad prison, which houses 1,250 people now (this detention center is not overcrowded, it is estimated that the number of places is consistent with the prison population). The third detention center is Canelones, which houses 1,110 people despite it can only house 750 places.

The Uruguayan government has planned and budgeted the building of 2000 additional places before 2015. This will substantially improve overcrowding conditions for the prison population.

Last week, a pre-feasibility study was submitted to the Government (Ministry of Interior) for a project to install a new prison complex at Punta Rieles, which will be done through the Public-Private Participation system. The call for bids is expected to be made in March. This initiative has already attracted interest, and queries have been made from Brazil, Chile, Mexico, the United States, Canada and Australia.

It is estimated that the awardee of the project will have to disburse US$84 million for construction of the prison, and that the works will take two and a half years. As of the opening of the facility, the private investor will collect from the Government an adjusted quarterly payment for twenty years –as indicated in the call for bids- estimated in the area of US$18 million per year.[15]

Of the transfers to be received by the investor, it is calculated that 50% will correspond to construction of the facility, 25% to meal expenses for 1,960 inmates, and 25% to other services. The only prison tasks that that Government will continue to perform are security, health care and rehabilitation[16].

b.2.2. Education.[17] Education is a fundamental right which realization plays a crucial role in developing countries as it generates greater equality, social inclusion and the promotion of the skills required for the incorporation of technical progress. Education has direct positive effects on economic and social welfare, productivity, income, employment and competitiveness.

[15] Data from www.observa.com.uy
[16] Ibid.
[17] Data from the website of the Ministry of Education and Culture www.mec.gub.uy

The study published by the Inter-American Development Bank (IDB) "*School infrastructure and learning in basic education in Latin America: an analysis from Serce*" concluded that Uruguay (together with Argentina and Chile) is one of the countries with better educational infrastructure.

The Bank recommends that for urban schools priority should be given to the construction of libraries, science laboratories and computer rooms or spaces for multiple uses. In rural areas, problems related to basic services must be resolved urgently.

For the coming years the Government is working on preparation of trusts to promote public-private investment. One of the most ambitious projects involving this system will be for improving and expanding education infrastructure. The plan promoted by education authorities will demand some US$130 million to remodel and build school facilities during the period. For this year six facilities are expected to be expanded and two schools are expected to be built[18].

b.2.3 Health.[19] The National Integrated Health System of Uruguay includes public and private sectors[20]. Uruguay has a wide geographical distribution of services with acceptable

[18] Data from www.observa.com.uy

[19] Data from the report of the Pan American Health Organization: Profile of the health systems of the Eastern Republic of Uruguay. Analysis and monitoring processes of change and reform. October 2009

[20] Several institutions compose the public health services sector. The network of health services of the Administration of State Health Services (ASSE) is the country's largest and includes hospitals, health centers and polyclinics. According to data from 2009, ASSE was covering a population of 1,192,580 people, approximately 36% of the Uruguayan population.
It is followed by the Armed Forces Health Service under the Ministry of Defense, which has its own hospital infrastructure in Montevideo, with 450 beds and nursing services in military units around the country. It provides coverage for approximately 250,000people (active and retired military and their families).
Thirdly, Police Health which is under the Ministry of Interior (Department of the Interior), has a 132-bed hospital infrastructure in Montevideo and, in the rest of the country, leases services from ASSE and private providers. It provides coverage for 70,000 people (active policemen, retirees and family members).
Additionally, the University of the Republic, through its "Hospital de Clinicas," covers part of the ASSE population and is currently operating with 450 beds.
There are also other health services on a smaller scale such as those offered by the Social Security Bank, Banco de Seguros del Estado.
The private sector includes IAMC (non-profit institutions), with 47 institutions providing people with prepaid comprehensive health services, 12 of which have their headquarters in Montevideo.
Most of these organizations have their own hospitalization services and their beneficiaries amount to 1,806,750 people. The institutions have from approximatley 3,000 to 240,000 members each.

levels of geographic access, because there are no major geographic or regional distances. Therefore, it could be said that every Uruguayan, to a greater or lesser extent, has access to health centers.

Since 2007, the rules for financing the health system in Uruguay have been amended creating a solidarity system of funding. According to estimates made by the various administrations that have been in charge of implementing this new system, it would be sufficient to meet the health needs of the population and they do not foresee special investments in this area for at least the short-term.

b.2.4 Housing. Uruguay has almost universal access to potable water, electricity, and sanitation facilities, as defined by the World Development Indicators.

It is one of the best positioned countries in terms of public access to these services. Still, when trying to achieve developed country level, Uruguay should focus on providing better services.[21]

In effect, the access to homes built on regularized lots is relatively high, while access to rural households in non-flooded areas is low, mostly due to poor coverage. And thinking in sanitation levels, meanwhile decreases to half when using a stricter definition of sanitation that best meets the standards in developed countries

Currently there are incentives from the government encouraging and promoting private investment in social housing (middle and lower middle income), mainly through the granting of tax benefits and guarantee funds.

Benefits will be awarded to projects that meet the conditions of improving financing and guarantees for the acquisition, lease or lease-purchase of affordable housing, as well as those promoting technological innovation in the area of building construction, contributing to social integration and using infrastructure services and equipment which has been already installed, facilitating access to housing of low , lower middle and middle

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There are also Private Insurance institutions which are private companies for profit. These insurers provide comprehensive care in a prepaid system including 74,789people.

[21] *WORLD BANK: URUGUAY: Equal opportunities - Achievements and Challenges, Report No. 57551-UY In December 2010.*

income sectors of the population, significantly expanding the amount of affordable social housing.

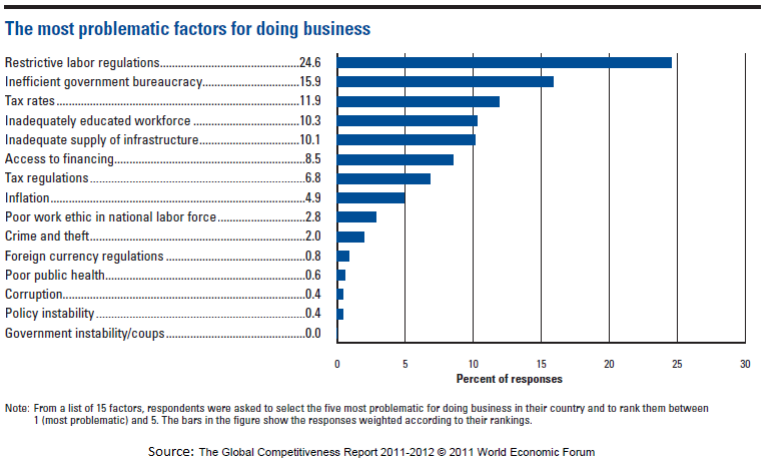
c. Uruguay in the world. In the last period Uruguay moved up to the 65rd position when it comes to the general situation in Infrastructure[22].

The figures in the WEF report are interesting: Uruguay is ranked 65 in what concerns the quality of roads, ranked 108 in terms of quality of the rail network, ranked 41 when it comes to port quality and 52 in what concerns the quality of air transport[23].

The reality of the Uruguayan infrastructure, its shortcomings, are among the factors considered by investors when analyzing the possibility of investing their capitals in Uruguay. According to the chart below, infrastructure problems are the fifth factor that hinders new ventures.

Known this reality, Uruguay cannot continue to delay investments in infrastructure in order not to stall the whole country.

Indeed, this demonstrates a real risk for the country since not changing this course can cause that the lack of "*infrastructure becomes a bottleneck to continue a process of sustained economic growth in recent years, thus creating an obstacle to promoting social and territorial cohesion, which is in the interest of the entire population*[24]***".***



[22] The Global Competitiveness Report 2011-2012, published by the World Economic Forum.
[23] The Global Competitiveness Report 2011-2012, published by the World Economic Forum.
[24] Appreciations in message and report of the Treasury Commission to the House of Representatives when submitting the PPP law project to study.

IV. Uruguay. State model. Role of government and private sector

a. Uruguay. Welfare State. For the purpose of living in society individuals place in the hands of the State many of our rights and freedoms for it to manage. Also we entrust it with the performance of certain activities and functions necessary for life in society to prosper.

Thus, each State is a reflection of a political reality that is determined by the relations between citizens and the Administration, within the boundaries that the citizens themselves establish. This means that each State, each Administration, has its own "administrative reality." This "administrative reality" is in each case composed of an integrated system of "State duties" aimed at the common good of the "citizens" who are under its sphere of protection.

The functions and duties[25] of the "administrative reality," which we call public administration,[26] will depend on the State model and will determine what kinds of activities will be assigned by law to the administration and how must they be executed.
Thus, the administrative reality of a liberal state with powers to make and enforce laws would be different from that of an interventionist state or benefactor, as was undoubtedly the case of Uruguay until recently, where the state was fully responsible for the social and economic welfare of its members, and was entrusted with all tasks in this regard.

b. A departure from the Welfare State? It is generally recognized that we are going through a transition from the interventionist or benefactor State, the shaper of economic and social order, to the so-called "Subsidiary State."

This transition arises as a response to the impossibility of the State to fulfill its assigned duties in an efficient manner. Although there are sectors (mainly within the union sector) that rise up against this state reform, there are increasing numbers of people who argue

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[25] Within the State's duties, there are different activities which are subsumed under different legal regimes in charge of the Public Administration. State duties include: i) regulation of private activity, ii) essential duties, iii) public services, iv) social services, v) performance of the state in the private sector, and vi) administration of justice.

[26] In Uruguay, the so-called "Public Administration" includes the three branches of government (Executive, Legislative, and Judicial), the Court of Accounts ("*Tribunal de Cuentas*"), the Electoral Court, the Administrative Claims Court ("*Tribunal de lo Contencioso Administrativo*"), the Local Governments, the Autonomous Agencies, the Decentralized Services, and the Public Education Entities.

that maintaining the old model is an undue burden on citizens, given that the results are not the desired ones and are a far cry from attaining a social welfare state, given the deficiencies and nonconformities. There is growing support for the position that the State's actions and the activities that must inevitably be carried out by it, as well as those that can be delegated to third parties, must be defined.

In our opinion, the State's actions must be focused on the so-called "essential duties" and those duties which involve a clear public interest, limited to the development of education, health, security and justice. Everything else should, to a greater or lesser extent, be delegated to the private sector, and strong and specific State controls should be established.

Accordingly, it is common to find concurring opinions affirming that economically profitable activities are not meant to be performed by the State, and should simply be controlled by the State to avoid potential private sector excesses, and that the State should only take part where private sector activities are not profitable, under the principle of subsidiarity (the State must only appear when the private sector can not comply successfully, and it must recognize the autonomy of social actors regarding the determination of their own objectives and the election of the processes to be implemented in order to achieve those objectives, notwithstanding the State's duty of control and performance of essential duties).

The withdrawal of the State from "economic life" goes along with the rethinking of the interventionist regimes given the great failures that States have faced as administrators. Consideration of the State as a poor administrator leads to effort to turn over certain activities to the private sector, seen in some respects as more efficient. To this end, the State has ventured into systems that combine the ability to delegate powers to privates, mechanisms promoting investments, creation of public figures outside the State's organization, Public-Private Participation regimes, among other solutions that point to the same end.

However we must not forget that in order to take that step back efficiently and achieve the desired results, it must be borne in mind that the State is not an end itself, but a "*submitted being,*" and both the State and all its entities are meant to "*serve and not to be served.*" The submission to which the State must be put is none other than to the common good of the

society it serves. If the organizational structure of a determined State fails to meet the purposes for which such structure was created, if it fails to achieve that common good, it must be amended, reformed.

The required modification of the actions of our administration must to be carried out through the application of "*a new order that takes place primarily by the elimination of barriers – deregulation – and the market operation by adopting open economic systems, with emphasis on competition*[27]*."* This will lead to "*a shrinking of the State with the abolition of monopoles and exclusive features regarding it, and the outsourcing of the public services whose ownership belongs to it, and those duties that do not derive from the unavoidable provision of the State.*"[28]

In Uruguay, this submission cannot ignore the "*limits resulting from the foundations of a state role based on the Constitution and solid general principles of law.*"[29] Thus, any reform of the State's activities must, in the first place, consider the constitutional provisions establishing the parameters within which our State's activity should be developed.

It will then be the legislator who, observing the constitutional precepts, will have to demarcate those activities that can be removed from the hands of the public entities and placed in private hands.[30]

V. Public-Private Law and investment in infrastructure

Ventures involving the association of public and private capital are not new to our environment. Historically, we coexisted with various public-private partnerships. In Uruguay we have different modalities and institutional negotiable modes[31] presented in

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[27] BRITO, MARIANO, in "*Desregulación sobre restricciones adminsitrativas a la competência*", in "*Estado-Administración"*, pg. 15

[28] BRITO, MARIANO, "*Las nuevas formas de gestión de los cometidos estatales*", in Administrative Law Annuary, Volume VI, pg. 9

[29] BRITO, MARIANO, Op. cit. note 24, pg. 11.

[30] CAJARVILLE PELUFFO, JUAN PABLO, "*Quehacer del Estado y actividad privada*", in "Estado-Administración", pg. 25

[31] DURÁN MARTINEZ, AUGUSTO – "Nuevas formas de relacionamiento público-privado en el cumplimiento de los cometidos del Estado", en Revista de Derecho de la Universidad Católica del Uruguay, 2009, Pg. 82. This paper provides a rich and detailed analysis of the various forms of public-private association. On the one hand, associations recognized as "bargaining mode," among which are concessions, are conducted under work and services contracts with private parties, trust funds, etc., implementing agreements for public works. On the other hand are those that can be qualified as "institutional modes," among which are semi-private companies subject to public law

the various forms of private and public relations that contribute to the purpose of complying with government duties.

However, it is understood that it should go a step further. The inefficiencies of the state in managing certain areas make it necessary for us to consider how we may, with the necessary guarantees, delegate certain tasks to third parties in order to obtain more efficient results.

In this way, and collecting the different findings of international law on the subject, on July 12, 2011 the Uruguayan Parliament approved Act 18,786. This act was known as the law on "public-private participation contracts for the performance of infrastructure and related services" (hereafter referred to as "Public-Private Law").

This new rule came to establish the regulatory regime applicable to the Public-Private Contracts, establishing a "new" private link with the State and shuffling elements of interest and the appropriate allocation of risk, assessment of best value for money, competitive dialogue, compulsory arbitration and sufficient guarantees to creditors.

a. Background. Public Companies Act. The question that prompted the enactment of the Public-Private Law had been raised in Uruguay for more than 20 years. In 1991 the Public Companies Act (Law 16,211) was approved, in the search for mechanisms for public-private partnership to meet the needs that the Administration could not cover by itself. This sparked an intense political and social debate on State Reform and the relevance of moving towards different types of "privatization" as tools for this.

The law was designed with the understanding that the State was not satisfactorily performing various activities. In the report submitted to the Senate by the Committee on Constitution and Legislation, several Senators expressed that "*the State does some things poorly, worse than private organizations under its administration, and that efforts to correct the defects do not have a profound result, or do so only for a short period,*"[32] causing the State to stop engaging in certain activities, especially in the social area, where it is hampered by not having the appropriate resources.

(subsections 1 and 2 Article 188 of the Uruguayan Constitution, semi-private companies subject to private law (subsections 3 and 4 article 188 of the Uruguayan Constitution) and non-state public persons.

[32] Senate Proceedings No. 92, Tome 338, May 28, 1991, pg. 200.

Alerted to this fact, the Public Enterprises Act was intended to promote a proposed policy, involving "*in some cases, reform (including increased State efficiency in certain areas, spurred by competition, through elimination of certain monopolies), and in others, allowing for the possibility of new legal forms, or even wholly private ventures, where experience (its own or that of third parties) has already shown conclusively not only that certain activities do not require direct state ownership, but that it produces persistently negative results (absolute or comparative) for Uruguayan welfare (thereby obtaining resources to devote to other purposes).*"[33]

Under this approach, the law envisaged abolition of several State monopolies and authorization for different agencies to merge with the private sector.

It also established a special procurement regime that allowed the Executive branch to delegate some activities. These activities were public services (which could be entrusted to third parties through permits or concessions), with the Administration reserving the right to supervise that the services are provided on a continuous, regular and efficient basis.

In addition to the above, the central government and autonomous entities and decentralized services were expressly authorized to contract or subcontract with third parties for the implementation of activities under their powers "*that do not constitute essential duties of the State or public or social services.*"

However, different sectors were against this law, which led several of its articles to be submitted to a referendum and repealed on December 13, 1992. Thus, contractual regimes established generally for different administrative bodies as well as the new legal framework for certain public entities became ineffective.

b. Context of the emergence of PPP: need for infrastructure now. Throughout Uruguay's history, infrastructure investment in the country was always entrusted to the public sector. Private participation in infrastructure projects has been low in comparison to other countries with similar characteristics.[34][35]

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[33] Ibid.

[34] WORLD BANK: URUGUAY INFORME DE POLÍTICA DE DESARROLLO (DPR) - *Eficiencia en Infraestructura Productiva y Provisión de Servicios Sectores de Transporte y Electricidad,* PAGE 81

In Uruguay, the origins of the Public-Private law are closely linked to the need to make infrastructure investments in order to cover the needs of this area that emerged over the years.

According to the explanatory memorandum accompanying the bill, Executive initiative was intended to "*give the public sector efficient mechanisms for contracting with the private sector in order to achieve the development of infrastructure and related services.*"[36]

The drafters of the law recognize that the development of infrastructure and public equipment-related tasks "*is an essential component for economic development and contributes decisively to increasing production and promoting social and territorial cohesion, which benefits the entire population*."[37]

They recognize that the reality of our country shows that the resources available to the State are insufficient to fund all the needs that have been deferred and must be met. Among the first needs that must be addressed are those that have been generated primarily in the areas of housing, education, health, prisons and transportation.

Given this fact, the drafters note that it is "*imperative to find ways to address the urgent need to make investments that will, in the short term, alleviate existing deficiencies ...*"[38] *and resolve, through this law, to promote public-private partnerships as an "efficient procurement mechanism through which the private sector applies its resources in the country, in the financing of infrastructure and related services*."

Thus, Public-Private Partnerships appear as a mechanism for private participation in infrastructure development in Uruguay.

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[35] Public sector investment in infrastructure has been constant at 98% of total investment in infrastructure for the period 1999 to 2006. Public sector investment in infrastructure has been composed by investment of government corporations (2/3) and the Ministry of Transportation and Public Works (MTOP) (1/3). WORLD BANK: URUGUAY INFORME DE POLÍTICA DE DESARROLLO (DPR) - *Eficiencia en Infraestructura Productiva y Provisión de Servicios Sectores de Transporte y Electricidad, pg* 81

[36] Bill of Law on Public-Private Participation in development of infrastructure and related services, submitted to Parliament by the Executive Branch (Matter No. 105,584)

[37] Ibid.

[38] Ibid.

c. Scope and purpose of the Law on Public-Private Partnerships. As mentioned, the Public-Private Law comes to establish the regulatory regime applicable to Public-Private Participation agreements.

These contracts are characterized as those in which the public administration entrusts a third party regulated by private law (contractor) for a given period, with the design, construction and operation of infrastructure or any of such benefits, as well as funding the same.

Under the constitutional boundaries, such contracts may be used for the development of infrastructure in the following sectors:

- Roads (including rural roads), rail, port and airport.
- Energy infrastructure (subject to certain regulations established by previous regimes and establishing some special procedures);
- Construction of waste treatment and disposal;
- Social infrastructure, including prisons, health centers, education centers, affordable housing, sports and improvement works, equipment and urban development.

Such contracts are also expected to be used for the colonization of land, which by its location, size and agricultural characteristics is economically suitable for population settlements.

On the other hand, a series of restrictions are established. In any case, Public-Private Participation agreements may include:

- Educational services in the case of schools;
- Health services in the case of health centers;
- Security services, health and rehabilitation of prisoners in the case of prisons.

Tasks that are to be provided exclusively by the State and activities conducted by monopolies established by law in favor of the State are excepted from this new contractual regime.

These contracts seek to have the private sector contribute with economic resources, knowledge and skills needed for development of projects so as to achieve "*the satisfaction of the public interest more effectively and efficiently*."

d. Some details of the procedure under the law. Although our Private Public Participation law does not innovate on comparative laws, we believe it is important to mention some of the features established for these agreements.

Agreements can be at the initiative of the Administration or of the private sector[39]. Prior to deciding whether or not to carry out such an agreement, the Administration should assess the feasibility and desirability of the project, for which a prefeasibility, feasibility and impact study must be presented. Moreover, a comparative analysis must be conducted with alternative forms of hiring to justify adoption of this hiring formula in technical, legal, economic and financial terms. In particular, it must be shown that the proposed procurement model allows the State to get the most "*value for its money*." As mentioned, it will only be possible to access these contracts if there is no other formula that offers greater benefits to the Administration and users.

Only once the assessment has been completed and the appropriateness of the project has been assured, can a public call be made in the form of a bid, auction, or any other mechanism permitted by current regulations.

A novelty to our system is the possibility of going through a competitive dialogue. For complex projects the Administration can use this mechanism to exchange confidential information with bidders responding to the public call for bids and complying with technical and economic solvency requirements. This “competitive dialogue” is geared to contributing to the best definition of efficient and viable solutions in the bidding conditions.

The competitive dialogue procedure will continue until the solutions that are appropriate for the purpose of the call are defined.

[39] Private initiative mechanism, allowing private parties to promote projects not yet considered by the government, in a framework that fosters such proposals and grants incentives to promoters through advantages in the subsequent competitive procedure.

The addition of the competitive dialogue is seen as a response to one of the disadvantages of contracting with the State at present: the lack of flexibility. The intention of this mechanism is for PPPs to create more flexibility for the State when hiring, regarding the definition of conditions, which will lead to some extent to improving the agreement to its own benefit.

Once the competitive dialogue is closed and all participants have been so informed, the State will announce its call for the submission of bids in line with the special conditions.

Bids must include all elements required and necessary for the project, and criteria for evaluating them must be fixed in advance. They may include various elements associated with the contract, such as quality, price, the formula used to adjust remuneration for use of the work or provision of the service, the execution time or delivery of the service, the cost-benefit assessment of financing, the satisfaction of social needs, profitability, value and technical suitability of the proposal, technical and economic soundness of the proposer, warranties, design or functional characteristics and any other relevant factor for the contract.

At that time, the provisional award will be made and will be communicated to all bidders. Any challenges will be analyzed, and then the final award will be made.

The next step is to formalize the contract. To prevent contracts from being a reflection merely of parties' will, the law establishes in detail the content that contracts must have. Among such content we emphasize the requirement that the conditions regarding risk sharing established between the contractor and the contracting party be clear, specifying the allocation of risks arising from the variation in costs or benefits, and the allocation of risks of availability or demand for such services. Contracts must also set the performance targets assigned to the private sector, especially in regard to the quality of services, supplies and works, and the conditions that must be made available to the Public Contracting party. These provisions are, among others, the establishment of an adequate control system that allows the public administration to verify compliance.

Finally, another important point to note is that the PPP law has determined that any disputes arising between the parties must be settled through arbitration under the Uruguayan Code of Procedure, and not to the local jurisdiction, or other international

arbitration mechanisms. The arbitrators may be determined in advance by the parties to the contract.

e. Advantages of using PPP. There are different elements, at least from a theoretical point of view, which lead us conclude that we should opt for investment projects in infrastructure as Public-Private partnerships. Following we review the most important elements that to our understanding could lead an investor to channel their investment through PPP.

e.1 Funds.[40] Evidently, realization of works of infrastructure generally requires payment of large sums of money. In Uruguay, the public sector is the main executor of major infrastructure projects, both through member agencies of the Central Government (Ministry of Transport and Public Works for example) and through the work undertaken by Public Enterprises (UTE[41], ANTEL[42], ANCAP[43] and OSE[44]).

From the financial point of view, the realization of large works has two major implications for public finances. The first is to obtain the necessary funds for these investments.

However, this would not be the main difficulty. The second relevant implication is the impact that these investments would have on the fiscal balance. Public sector accounting in Uruguay is not kept on an "accrual basis" but instead on a "cash basis." This implies that the funds invested in infrastructure are not integrated as part of the asset but are recorded as a loss for the year in which the cash outflow was recorded, and hence increase the fiscal deficit. For example, if works were executed in 2012 for USD 2 billion, this cost increase would generate a fiscal deficit of about 2% of GDP, which added to the deficit as projected by the government (approximately 1% of GDP) would leave Uruguay with a fiscal imbalance of 6% of GDP, a figure that could affect the market's credibility in the sustainability of public finances.

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[40] Information provided by CPA / FERRERE Consultants - Economist Alfonso Capurro
41 National Electric Power Plant and Transmission Administration (UTE).
[42] National Telecommunications Administration (Administración Nacional de Telecomunicaciones - ANTEL)
[43] Fuel, Alcohol and Portland National Administration (Administración Nacional de Combustibles, Alcohol y Portland – ANCAP)
[44] National Administration of Sanitary Works (Obras Sanitarias del Estado – OSE)

The PPP law is presented as a possible solution to these problems. Through private investment the disbursement is not initially recorded on the public sector accounts.

However, for this solution not to be a problem in the future, since under PPP the cash disbursements begins as from when the work is in operation and not before, [45] the Administration should not ignore the evaluation of the budget liability involved in a PPP project. Failure to perform this evaluation from the outset for PPP contracting can mean that future contingencies will be passed along to future Administrations without the latter having estimated the fact that they would have to deal with them.[46][47]

In addition of those provisions, the PPP law limits the flow of projects that can be performed using this mechanism to 7% of the previous year's Gross Domestic Product (GDP). In turn, the expenditures of the State using this mechanism cannot exceed 5 per 1,000 of GDP per year.

e.2 Efficiency. There are different reasons that lead us to conclude that Governments are unable to manage public enterprises and most public services in an efficient way.

This inefficiency is rooted in partisan political interests among those holding power and making decisions, the tendency to not use public enterprises for commercial objectives, the enormous bureaucracy Uruguay suffers, and an over-empowered union system, among other factors.

Whatever the cause, inefficiency means that many utilities that provide infrastructure services are over-staffed and badly managed, to the detriment of consumers and society as a whole, and private investments appear as an alternative for this situation.

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[45] Treasury Commission of the House of Representatives File No. 485 of 2010 – Stenographic Version No. 360 of 2010. Session held on December 1, 2010.

[46] In analyzing the "cash flow" the legislature understood the forecasts established to prevent failures at this point. Thus, it established tools to assess the contingencies and other liabilities to pay and define the accounting treatment to be given. Also established limits on the amounts of these items that the State can assume and the controls exercised by Parliament (see Article 60, Law 18,786).

[47] CAF Report on "*La vinculación del capital privado en el desarrollo de proyectos de infraestructura de transporte y energía en la República Oriental del Uruguay*," Volumen I, pg. 33.

The private sector can improve performance even in very difficult situations. The private sector has a different conception of doing business, and always tries to "win," to obtain the best value for money, all of which implies being efficient.

In addition, being efficient is required by the Public Private Participation law. When we talk about "efficiency" as a principle that we must follow we need to know that the term comes from economics, and means that a party is efficient if it can produce a good or provide a service at the lowest possible cost.[48] It is clear that the concept of efficiency must be understood in a broad sense,[49] including effectiveness notions (accomplishment of objectives and goals) and efficiency (lowest possible cost).[50]

e.3 Transfer of risk and "Value for Money."[51] The PPP law itself includes, among its principles, "adequate risk distribution." According to this principle, contracts must provide adequate distribution of risks between the Private Party and the State, so as to minimize the costs associated with such risks.

This type of contract must analyze all possible variables and risks involved in the infrastructure project to be carried out, and attribute those risks depending on which party is in better position to face and mitigate them if necessary.

Beyond the particularities that may arise in each case, risks involving costs, delays, adequacy of design, construction, problems with the staff working on the site, among others, are usually attributed to the private parties. Private parties will not charge in excess of the price, even if the work costs are higher than originally projected. Consequently, the private party will not charge for the service as long as it is not providing same, or if the service does not meet the agreed standards.

The same occurs whenever risks are attributed to the State. Once, for example, a price payable by the State to a private party once the services begin has been agreed, the private party will not receive less if the use of such services is not in line with the State's projection.

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[48]CORREA FREITAS, RUBEN, "*Los principios constitucionales de la función pública*" in "*Manual de la Función Pública"* by CORREA FREITAS, RUBEN and VAZQUEZ, CRISTINA, FCU 1998, pg. 12.
[49] CORREA FREITAS, RUBEN, Op. cit. pg. 15
[50] CORREA FREITAS, RUBEN, Op. cit. pg. 15.
[51] Echeverría Petit, José Luis, Op. cit., pg. 8.

Thus, if each risk is borne by the party most suited to cope with it, in the most efficient or economical manner, the risk is reduced and the cost will be lower. This allows for resources not to be wasted and for obtaining the best possible return on the investment, greater economic efficiency, and the highest value for money.[52]

e.4 Definition of obligations such as service standards and fostering of innovation.[53] In Public-Private Participation contracts a specific outcome and a specific compliance standard are sought. The latter because, unlike other agreements such as public works contracts, the focus in this contracts is on the service and not on the work itself.

We strongly believe that this is an advantage, since it goes a step further on what is entrusted to privates, and an increased commitment of the latter is achieved. The private sector will have to show inventiveness and creativity in order for the work to achieve a certain "service" provision in order to fulfill the needs for which the same was requested.

This, without a doubt, encourages innovation. Innovation will be fostered as long as the privates agree to comply with certain results, certain standards for which they will have to obtain the best cost-benefit ratio, for which it is necessary to innovate.

e.5 Collaboration.[54] For a venture carried out through a PPP project to be successful it is imperative to have the cooperation of both parties (public and private). The fate of the project will matter to both parties, and will require the sincere commitment of both parties to the project in order for it to be executed efficiently and according to the highest quality standards.

VI. Conclusions

As noted several times throughout this paper, Uruguay is experiencing strong economic growth, to an extent not seen since the 1940s. The levels of investment in Uruguay are in the area of 20% of gross domestic product, while foreign investment levels are the highest in recent years.

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[52] 'Value for money' is a term used to assess whether or not an organization has obtained the maximum benefit from the goods and services it both acquires and provides, within the resources available to it.
[53] Echeverría Petit, José Luis, Op. cit., pg.8
[54] Echeverría Petit, José Luis, Op. cit., pg.8

In this framework, the country's main challenge in the short term is to lift the restrictions on infrastructure. This will allow Uruguay to apply innovation, efficiency and productivity to economic activity, which will yield a market that is more appealing to investors, whether domestic or foreign.

Recognizing this urgent need, a law was passed establishing the framework for entering into contracts for public private participation with a view to facilitating investment in infrastructure.

This law introduces new mechanisms through which private and public sectors can work together to obtain the best possible infrastructure project: the most profitable for the private party, the most advisable for the administration, and the most beneficial for users of the services provided. At least, that is the intention of those who supported the new legislation.

Nevertheless, the results to date to not seem to be what was expected. The implementation of Public-Private Partnerships projects has been slower than expected, which is disturbing to all those who understand the urgency of investing in infrastructure.

Indeed, it has been over half a year since the law was passed, and what has materialized so far is, in our opinion, insufficient. This has been evaluated by the authorities who in public have shown great concern about this issue.

These concerns led to drafting of an Executive decree regulating the law, which is expected to be published in the coming days. This decree aims to make some of the criteria established in the law more flexible and, above all, to speed up some of these procedures.

Although some projects would seem close to materializing (prisons and highways), the current situation does not allow us to extract sufficient evidence to conclude whether this law will be useful or not, if it will make a difference, and if it will be the vehicle needed to get beyond the status quo, necessary for the Uruguayan economy to continue growing.

Yet, what we dare to assert, beyond the necessary adjustments that ought to be made and future regulations, is that the main advantage that our society obtains out of this law is the mitigation of the stigma that private capital faces in countries like ours.

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