

Public Private Partnership: Case of Bosnia and Herzegovina

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ABSTRACT

Public Private Partnership (PPP) is a contract between the public and private sector. The goal of PPP is to deliver public goods in fields such as infrastructure, transport, communication, health, education, and social services. It is up to the private sector to provide a public good or service using superbly efficient project management methods while accepting a big part of the financial, technical and operational risks in the project. The PPP model started to be widely applied in the early nineties of the last century, mainly in Great Britain, Canada, Australia, the United States, China, and India. It was seen as a good model for implementation of big, long lasting infrastructure and other projects, using mainly private investment. Governments consider this model favorable, as it enables implementation of huge projects without spending money from the budget or borrowing, and preferable in comparison to public purchasing. PPP projects might satisfy the needs of citizens (tax payers) with regards to water, housing or electricity. The UN declared that world poverty would be eradicated by the next generation through the application of the PPP model in the area of water supply, electricity, health and education. This model could be a good solution for countries in the region, and particularly for Bosnia and Herzegovina. The necessary investments in infrastructure, health, education and social projects cannot be financed solely from the budget. Budgets in BiH are limited, as a result of the current economic situation, increasing public debt, constant budget deficits and pressure from the International Monetary Fund. Researchers from the government, business, and financial sector, as well as international organizations, have shown high interest to study the PPP model. As far as the research methodology is concerned, a thorough literature review of secondary data sources was conducted in order to draw the current conclusions and make recommendations for the future. Upon assessment of the current situation in Bosnia and Herzegovina regarding the PPP model, the authors will propose solutions for the implementation of a functional PPP system in order to increase economic growth and provide better services for citizens.

Keywords: Public Private Partnership, Infrastructure, Public Sector, Private Sector.

INTRODUCTION

Public Private Partnership (PPP) is a contract between the public and private sector. The goal of PPP is to deliver public goods in fields such as infrastructure, transport, communication, health, education, and social services. It is up to the private sector to provide a public good or service using superbly efficient project management methods, while accepting a big part of the financial, technical and operational risks in the project.

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This model could be a good solution for countries in the region, and particularly for Bosnia and Herzegovina (BiH). The necessary investments in infrastructure, health, education and social projects cannot be financed solely from the budget. Budgets in BiH are limited, as a result of the current economic situation, increasing public debt, constant budget deficits and pressure from the International Monetary Fund.

Researchers from government, business and the financial sector, as well as international organizations agree that a functional PPP system might increase economic growth and provide better services for citizens. However, establishing and implementing a PPP system in a country is challenging. PPP projects are long term projects, very expensive and very complicated. They are complicated from the legal, financial and technical point of view. They require a long planning and specific knowledge in different fields. They bear a substantial risk in all phases of the PPP project cycle. The success of a PPP project is largely determined by adequate risk assessment. One of the biggest PPP risks is precisely inadequate risk analysis. In the case of unrealistic assessment economic and social consequences that the realization of a particular project results in, can be extremely negative for the region and the state.

The Economist (2013) grouped Eastern European countries in terms of their environment for sustainable, long-term PPPs. The groupings cover four broad levels of development: mature, developed, emerging and nascent. No country in Eastern Europe can be strictly classified as mature in terms of PPP readiness and capacity, although Croatia and Slovenia fall into the developed country category. Almost two-thirds of the countries in the study including Albania, Croatia, Bulgaria, FYR Macedonia, Montenegro, Romania and

Serbia can be considered emerging in this respect, denoting a region whereby significant progress in PPP readiness has been made, but ample room for improvement remains. BiH is the only country in the region that falls in the nascent group. There are no PPP projects in BiH, although there are projects with some elements of PPP. There is huge interest from local communities to solve their infrastructure, health, education or social problems with the PPP scheme, but none have been implemented. It is necessary to analyze the environment for PPP in BiH, as well as previous PPP project proposals to figure out why there are no such projects despite great interest.

LEGAL ENVIRONMENT FOR PPP

Every country aiming to attract the private sector to the PPP system has to firstly ensure a sound legal environment for PPP. The private sector, as well as financial institutions, has to have high certainty that their legal right will be protected before they make long term obligations. In the case of BiH which aspires to join the EU, all this legislation has to be harmonized with the relevant European Union *acquis* and best European practices. This includes the Procurement Directive, notably the Directive 2004/18/EC on Public Works and Services Concessions, the Utilities Directive 2004/17/EC, the EU Green Paper on PPP (Green Paper on Public-Private Partnerships and Community Law on Public Contracts and Concessions, COM (2004) 327 final). BiH also has to follow other relevant EU policy, such as principles of EU funding (structural funds, regional development funds, and social funds) since it seeks to enter the EU in the future and aims to comply with major EU funding principles from the outset. The European Commission Interpretative Communication on Institutionalized PPP, C (2007)6661 and the concept of the Competitive Dialogue introduced by Directive 2004/18/EC might also be of particular interest.

BiH has a highly decentralized administrative structure. According to the Constitution, BiH consists of the State of BiH, the Federation of BiH (FBiH), the Republic of Srpska (RS), the Brcko District (BD) and ten cantons. Economic activity is the responsibility of the entities and cantons, and thus PPP matters are also the responsibility of the entities and cantons. The following laws in BiH regulate PPP matters:

Law on PPP in RS published in Official Gazette of RS, No 59 in 2009

Law on PPP in BD published in Official Gazette of BD, No 2/10 in 2010

Law on PPP in Canton Sarajevo published in Official Gazette of Canton Sarajevo, No 27/11 in 2011. This Law was amended in 2017 and changes are published in Official Gazette of Canton Sarajevo 16/17.

Law on PPP in Herzegovina-Neretva Canton published in Official Gazette of Herzegovina-Neretva Canton, No 02/13 in 2013

Law on PPP in Central Bosnia Canton published in Official Gazette of Central Bosnia Canton, No 13/13 in 2013

Law on PPP in Una-Sana Canton published in Official Gazette of Una-Sana Canton No 19/12 in 2012

Law on PPP in Posavina Canton published in Official Gazette of Posavina Canton, No 04/13 in 2013

Draft Law on PPP in Canton 10 in 2016

Law on PPP in Tuzla Canton published in Official Gazette of Tuzla Canton No 14/12 in 2012

Law on PPP in Zenica-Doboj Canton published in Official Gazette of Zenica-Doboj Canton No 06/16 in 2016

Law on PPP in West Herzegovina Canton published in Official Gazette of West Herzegovina Canton No 14/13 in 2013

Law on PPP in Bosnian-Podrinje Canton published in Official Gazette of Bosnian-Podrinje Canton No 05/13 in 2013

There are laws on PPP in RS, BD and almost all cantons. There is no Law on PPP, however, on the level of the FBiH; a draft PPP law is under discussion in the Parliament. The Ministry of Transportation and Communications sent a PPP draft law to procedure several years ago, but it was rejected. They sent a new version again three years ago. There is also no Law on PPP on the BiH state level. PPP, by nature, needs the involvement from the BiH state in some shape. However, there is strong opposition from RS to any frame law or any involvement of State level in PPP matters.

Besides the laws on PPP, there are a number of other relevant laws and regulations addressing this topic in BiH, especially those on concessions. Hence, it can be concluded that there is a legal environment for PPP in BiH. All laws state that they are harmonized with the EU legislation, Green paper on PPP, EU procurement rules and best EU practices. Nonetheless, all these laws should be carefully reviewed, compared and analyzed to determine if they in fact are harmonized with the EU acquis. Further, the legal environment for PPP has to be improved by adapting PPP legislation on the level of the BiH State and FBiH.

INSTITUTIONAL ENVIRONMENT FOR PPP

The Ministries of Finance are in most cases the institution responsible for PPP. There are also Committees for Concessions at the level of the BiH State, FBiH and RS, which are sometimes involved in PPP matters. The Committee for Concessions at the level of the BiH State is the most active in the field of PPP. There is an Agency for PPP at the BD level. However, all these institutions are understaffed. They lack people, financial resources, and knowledge on PPP. Research done by the Regional School on Public Administration (RESPA, 2015) shows that the majority of institutions responsible for PPP development in the Western Balkan countries do not provide any trainings on PPP issues (Albania, BiH,

Macedonia, Montenegro and Serbia), with trainings being provided only in Kosovo. Employees in the public sector complained that the lack of PPP training is the main obstacle in implementing PPP projects in BiH.²⁰

There is no Central PPP unit at the level of the BiH state. The Economist (2013) states that international best practices demonstrate that some level of centralization of expertise is conducive to a well-functioning PPP system, even if implementation remains fragmented along sectoral lines. Although there are examples of global PPP leaders, such as the UK, moving away from a centralized model over time, it is important to note that the country started out with a centralized PPP Unit at the beginning of its private finance initiative programme, and built up capacity over decades before changing the institutional model. It is necessary to have PPP specific expertise within government agencies. This expertise is key to ensuring that risks are allocated properly, financing is sourced and structured appropriately, analyses of value for money and feasibility are prepared well, and that a country's ability to handle litigation in the construction phases of projects is adequate. A central PPP unit would advise and coordinate PPP activities between all administrative levels. The PPP unit would serve as a pipeline for EU grants regarding PPP matters. The RS strongly opposes the establishment of such a unit at the moment.

PPP PROJECT PROPOSALS

In order to determine why there are no PPP projects in BiH, a few PPP project proposals will be analyzed. All these proposals come from the RS (Government of RS, 2013). The RS is the most advanced part of BiH in terms of PPP. The RS adapted the Law on PPP in 2009 and amended it in 2011 (Official gazette, No 59/09, 63/11). It also enacted other regulation regarding PPP like the Decree on the procedure for the implementation of public-private partnership projects in the Republic of Srpska (Official Gazette of Republic of Srpska, No. 104/09, 62/12) and Rulebook on the content and manner of keeping the register of public-private partnership projects in the Republic of Srpska (Official Gazette of the Republic of Srpska, No. 32/10).

The institution responsible for PPP is the Ministry of Finance. The basic competencies of the Ministry relate to the assessment of the justifiability of the proposed project and the assessment of the justifiability of the proposed PPP model. The Ministry also gives an opinion or issues a decision (depending on who is the public partner) on the compliance of the final draft of the contract with the proposal of the PPP project, the tender documentation and the provisions of the regulation. The Ministry of Finance keeps the Register of approved projects and projects that have not been implemented, proposes amendments to the laws and bylaws and regulations important for the implementation of best practice in the preparation and implementation of PPP projects, gives expert opinions, and provides instructions for the preparation, implementation and monitoring of projects.

²⁰ Authors have interviewed public servants in ministries of finance and committees for concession during preparation of the TOR for the project of implementing PPP in BiH, financed by the PAR fund

The line ministry submits to the Ministry of Finance an opinion on the study or pre-study of economic feasibility as well as an opinion on the compatibility of the project proposal with sectoral development plans and strategies or regulations. Moreover, the relevant ministry gives consent on the conclusion of a public-private partnership contract in cases when the public partner is a local self-government unit, a public institution founded by a local self-government unit or a publicly-owned enterprise under majority ownership of a local self-government unit.

The Government of the RS considers the Project proposal information submitted by the Ministry of Finance and makes a conclusion by which it accepts the proposed model of realization that relies on the PPP model or requires that the proposed project be implemented using another model.

Prior to any development and project proposal, the duty of a public partner is to develop a feasibility study, which, together with accompanying documentation, is submitted to the Ministry of Finance and directly to the relevant ministry. It is important to note that only an authorized public partner has the authority to submit a project proposal, therefore there is no legal possibility for the proposal to be submitted by an interested private partner.

Several PPP health sector projects have been submitted to the Ministry of Finance of the RS in accordance with the procedure prescribed by Law. The proponent of the projects was the Ministry of Health and Social Welfare. One such project proposal included construction of the Center for cardio surgery. The economic justification study of the construction and equipping of the Center for cardio surgery indicated that there were no cardiac surgery departments within the clinical centers in the RS. Therefore, patients were forced to travel to other countries in the region. They primarily went to Serbia, but also to the FBiH and other foreign countries. Patients had to wait for heart surgery at the clinics in Serbia from a few months to over a year. So, the main reason for building of the cardio surgery hospital was the huge need of patients for such kind of medical services. Another reason was the need for the health system of the Republic of Srpska to be improved and expanded with cardiac surgery, which should have resulted in a number of additional benefits, such as:

- Training own medical and specialist staff,
- Contribution to the development of education in medicine in the RS, primarily at the medical faculties,
- Defining their standards in the field of cardiac surgery and their adaptation to the highest standards in that field in the EU,
- Contribution to the development of prevention of heart and blood vessel disease in the Republic of Srpska,
- Scientific monitoring of the heart diseases of the population of the Republic of Srpska and identification of the main causes, and defining a program for their elimination,
- Reduction of waiting time for surgery,

- Savings in patient transport costs,
- Improvement of postoperative control of patients.

This project failed. The Ministry of Health and Social Protection canceled the project. The explanation stated that the public partner and the selected private partner did not fulfill the conditions stipulated in the tender documentation. The public partner failed to provide the location conditions for the construction of the facility and the private partner failed to provide the bank confirmation of financial resources needed for the project's implementation.

Two other PPP health care projects were not implemented although their procedure started in 2011, namely the projects of constructing and equipping the centers for dialysis in Trebinje and Foca. According to the study developed the primary reason to build and equip such centers was the great need of patients for such types of medical services. Granted, there are dialysis centers within the general hospitals in Trebinje and Foca. However, in both cases, they are located in one room that does not meet the minimum standards for provision of dialysis services. Additional benefits the study lists would have included education of own staff, getting modern equipment, satisfying public needs with high quality service based on local prices, opening new working places.

The Bijeljina municipality proposed the construction of a port on the river Sava on the territory of the municipality. The project proposal was submitted to the Ministry of Finance, the Ministry of Transport and Communications and the Ministry of Agriculture, Water Management and Forestry in 2011. The financing, construction, equipping, organization, operations, maintenance and services for the port should have been done via the PPP model according to proposal. The private partner should have participated in investments with 80% of the investment value. The municipality of Bijeljina would have provided the land and the amount of contributions, fees and taxes for these facilities totaling the remaining 20% of the value of the investment. The private partner would have been obliged to construct the port, to provide continuous services according to defined standards, to perform maintenance and to concede the facility to the ownership of the public partner after the expiration of the contract.

According to the study, the primary reason for the construction of the port laid in the great opportunities provided by river traffic and the importance of the Sava River as a waterway for the economies of the surrounding countries. Other benefits would include the construction of a new port building, meeting public need with a high quality service, opening of 30 new working places and transfer of real estate to the ownership of the public partner after the expiration of the contract.

Yet, during the negotiations, the private partner stated that it would not accept transfer of the port facilities, equipment and related industrial infrastructure to the public partner.

All PPP legislation requires the transfer of all assets built for the realization of the PPP project to a public partner after the expiration of the time period stated in the contract with the private partner. In this case, the private partner's requirement to keep the assets after the expiration of the contract was against the PPP definition and, accordingly, the legal

provisions. So, the public partner decided to suspend the realization of the project using the PPP model. Ultimately, the public partner decided to realize this project in another way.

The University of Banja Luka submitted a study to the Ministry of Finance and the Ministry of Education and Culture for the establishment of a business-educational center which would provide digital printing services, upon which a PPP procedure was initiated by the public partner. The economic justification study defined the obligations of the public and private partners in frame of the proposal for this project. The obligations of the private partner were:

- Adaptation of Faculty of Technology premises for the business-educational center
- Equipping the center
- Operational management of the Center
- Maintenance of the Center
- Production of all materials
- Market research and material distribution
- Providing services to the public partner in accordance with the contract
- Providing services to third parties on a commercial bases
- Reporting to the public partner
- Transfer of property to the public partner

The obligations of the public partner were:

- Provision of premises at the Faculty of Technology for the functioning of the Center.

The Municipality of Doboj, as an authorized proposer, submitted the project proposal for "Construction of a sports hall in Doboj" to the Ministry of Finance, to be realized through the public-private partnership model. The proposal treated financing, construction, equipping, organization, commissioning, maintenance and provision of services, relating to the construction of the sports hall. The private partner would participate in infrastructure construction investments, while the municipality of Doboj would participate with the land, settlement of property legal matters and completion of the project documentation. The economic analysis carried out by the municipality showed that the private partner could not make a profit through this model. The Municipality of Doboj concluded that there was a lack of money for the investment, but that, nonetheless, the determining factor should have been public interest. However, the Ministry of Finance still found this project not justifiable, being that the risks associated with project realization and the lack of profit, would not reflect the private partner's interest. The Ministry then informed the RS Government about the conducted economic analysis of the proposal, based on which the Government decided

against the proposed model of realization, but still left open the possibility for the municipality to try to implement the project using another model

The regional landfill in Bijeljina, a public enterprise, submitted to the Ministry of Finance, the Ministry of Spatial Planning, Construction and Ecology, a study on the economic justification for the construction of facilities for separation of solid municipal waste at the Regional sanitary landfill "Brijesnica" in Bijeljina, with which a public-private partnership procedure was initiated by the public partner. The economic justification study for construction of a plant for the separation of solid municipal waste determined the obligations of the public and private partners. The obligations of the private partner were:

- Financing construction and equipping of the center for the separation and treatment of municipal waste
- Separation of secondary raw materials from municipal waste,
- Treatment of waste by a mechanical method,
- Sale of treated waste to recyclers,
- Continuous provision of services,
- Responsibility for the cost of defined maintenance, use and management,
- Submission of the facility to the ownership of the public partner after the expiration of the contract.

Obligations of the public partner were:

- Providing the land for the construction of a center with all necessary permits,
- Providing the utility infrastructure,
- Transporting the total collected waste to the treatment in the center.

This project proposal is still in procedure.

The public enterprise "Autoputevi Republike Srpske" (Republic of Srpska Highways) started a public-private partnership procedure by submitting the proposal for the project titled "Public-private partnership project in the construction, financing, use, maintenance and management of the section of the Doboj-Vukosavlje highway (part of the corridor Vc going through the Republic of Srpska)". The proposed model implied that the generated revenues were not sufficient to attract a private partner. In other words, a private partner would not be interested in implementing the mentioned project. Analyses carried out by Deloitte Center Europe Limited show that the projected traffic flow for the Doboj-Vukosavlje stretch was not sufficient to compensate for the costs of financing, maintenance, construction and management of that part of corridor. The analyses also concluded that an increase in the duration of the contract would not be seen by a private partner as sufficient compensation, to accept the risk of insufficient traffic flow. The project proposal proposed that the public

partner take on the risk of demand, which in the specific case means that payments to the private partner would be guaranteed by the government by way of revenues generated through other motorway sections and from the excise tax on oil derivatives.

However, the public attorney warned that the prerequisite for the conclusion of the contract was the completion of the real estate expropriation procedure for the parts of the Corridor Vc stretching through the Republic Srpska. The public attorney stated that any future contract would not be valid without solving these legal property matters with the legal owners. This project is still in procedure.

A few projects implemented in RS before adoption of the Law on PPP had some elements of a PPP model as the cooperation between the public and the private sector was used as a way of financing public needs. These projects were in the field of health care, such as establishment of dialysis centers in several cities and the Center for Radiotherapy located within the Banja Luka Clinical Center. Unlike PPP projects implemented after the adoption of the Law, contracts signed in the previous period do not oblige the public partner to submit reports to the line ministry and Ministry of Finance, nor are these contracts kept in the Register. Therefore, it is not possible for the line ministry and the Ministry of Finance to supervise and monitor these projects; rather it is the responsibility of the contracting parties. All these projects were initiated by the private sector. The main characteristic of a PPP model is that the public partner initiates the PPP procedure. The legal provisions in all PPP laws state the same. Yet, a lot of media indicated that the public partner has been paying from the budget much more than agreed. Research on PPP (Uzunovic & Karkin, 2014), financed by the Open Society Fund Bosnia & Herzegovina concluded the same.

It is clear from all these cases that there is huge interest from local communities, public companies and universities to solve problems like ports, roads, sport centres, landfills, building hospitals or specialized medical centres inside existing hospitals. There is also much pressure on local communities to solve all these problems and improve the quality of life of their citizens. However, budgets are always very limited. Local communities look at the PPP model, expecting to solve all these problems without spending money from the budget or by spending limited amounts of money. In many cases, local communities offered land or existing facilities as well as services that are in their competencies.

It is obvious from all these cases that public partners lack knowledge on the PPP model. A public partner should take care about the public interest and satisfying the needs of citizens. However, the goal of the private partner is to make a profit. The Municipality of Dobož proposed building a sport hall through the PPP model, although it was clear from its economic study that the private partner could not make profit on that investment. It is not realistic to expect that the private partner would only care about the public interest. It is also not realistic to expect from the private partner to compensate the lack of public funds without earning any profit. In several cases, the public partner entered in a PPP proposal without enough planning and before solving the preconditions for the PPP model.

Private partners also lack the knowledge on PPP. In the case of the port in Bjeljina, the private partner stated during the negotiations that he would not accept the transfer of the port facilities, equipment and related industrial infrastructure to the public partner. It is obvious that the private partner did not understand the PPP model. In other cases the private partner went into negotiation without providing financial means.

It is important to know that PPP is one of the models of financing public projects like infrastructure, roads, airports, ports, water supply, waste management, building hospitals, sport centers, schools etc. It is better to finance public projects by public procurement models in some cases. The main criteria for making decisions is to apply the “value for money” principle in order to determine what model will give more value for tax payers’ money (Juricic & Marenjak, 2016). PPP contracts in RS, that have been undertaken before the Law on PPP came into effect, additionally burden the budget.

PPP procedures are very long. It is evident from experience in the RS that several years had to pass before any decisions regarding PPP projects were made. Every phase in the PPP project cycle (project preparation, assessment, procurement, implementation and monitoring) requires special care and takes a lot of time. Lack of PPP knowledge and experience both from the public and private side can make the whole process even longer.

CONCLUSION AND RECOMMENDATIONS

The PPP model might be a good solution for BiH for financing the necessary investments in infrastructure, health, education and social projects. Local communities and public companies demonstrate a great interest for PPP as budgets in BiH are limited, as a result of the current economic situation, increasing public debt, constant budget deficits and the International Monetary Fund’s pressure. State and entities demonstrate lesser interest for PPP. Several measures have to be undertaken in order to build a functional PPP system in BiH, in accordance with the relevant European Union acquis and best European practices. Because of the highly decentralized administrative structure of BiH, it is necessary to establish and implement an efficient framework for PPP at the levels of the BiH State, FBiH, RS, cantons and BD. It is necessary, in the first place, to develop the legislation in the domain of PPP and harmonize the existing legislation regarding PPP in BiH. The Law on PPP should be adopted at the BiH State level.

However, creating an effective PPP system requires more than just passing the necessary laws and making regulatory changes. A successful PPP system requires institutions with specific expertise in PPP project cycle management, experience in risk identification and management, as well as sector and project oversight. There are institutions at almost all administrative levels in BiH that deal with PPP matters. Ministries of finance are in most cases the institutions responsible for PPP, what is a good solution. There are also committees for concessions at State and entity levels. It would be beneficial to create a PPP central unit at the BiH State level with the task of coordinating, advising and serving as a pipeline for EU grants regarding PPP matters. However, all these institutions are understaffed and lack special PPP knowledge. Key PPP institutions should get human and financial resources.

PPP projects are long term projects, complicated from the legal, financial and technical point of view. They require long planning and specific knowledge in different fields. They bear a substantial risk in all phases of the PPP project cycle. Success of the PPP project is largely determined by adequate risk assessment. One of the biggest PPP risks is precisely inadequate risk analysis. PPP contracts can additionally burden the budget under unrealistic consideration and evaluation of the conditions for payment of debts to the private sector. In that case, the consequences for the budget deficit are long-term. Hence, it is of the utmost importance, after setting the institutional and regulatory environment, to build and train capacities in the relevant institutions for the preparation, implementation and oversight of PPP, and thus, intensive trainings should be organized.

Private sector should be trained and educated about the opportunities and possibilities for businesses under a PPP scheme. A favorable environment for businesses as well as financial organizations participating in PPP schemes should be created. In the case of unrealistic assessment, economic and social consequences that the realization of a particular project results in can be extremely negative for the region and the state. The wider public should be also educated about the advantages and disadvantages provided by PPP.

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