

## Client Alert: Liberalization of Egypt's Railway Sector

By Khaled Ragheb

*In April 2018, Egypt abolished the state monopoly on ownership and operation of its railways. This Client Alert examines the opportunities and challenges for private sector investment in the Egyptian railway network.*

On April 2, 2018, Law No. 20 of 2018 (“**Law 20/2018**”) was published in the Official Gazette. It amends certain articles of Law 152 of 1980 which established the Egyptian National Railway (“**ENR**”) and enables the private sector to actively participate in the operation of the railway network, and all other associated aspects. The catalyst for this new law is the desire of the Egyptian government to encourage the private sector to participate on a much larger scale in the rejuvenation of the Egyptian railway sector over the coming years.

The first Egyptian railway line was developed as early as 1835 and, historically, Egypt was the second nation to develop a railway system after England. However, today, the railway network is in a critical state. Most lines have been severely ill-maintained over many decades which has caused a number of catastrophic incidents. The Egyptian government has not embarked on any meaningful comprehensive renovation of the network since its inception and/or effectively address the deep-seated dysfunctions of the sector. Due to its poor reputation, the railway sector has become a constant source of embarrassment for successive governments.

Recently, due to the increasing pressure on officials to restore a decent and safe level of service to passengers, a debate has raged, within and outside of parliament, as to the inevitable need of involving the private sector in the future operation of the railway network. Proponents of private partnership highlight the key chronic illnesses of ENR, and the sector as a whole: (i) lack of competent manpower, (ii) lack of adequate financial capabilities to upgrade the network, (iii) dismal level of service, (iv) continuous losses on the balance sheet, and (v) failure to maintain assets in proper condition. The President himself lately stated that investments ranging between 200 to 250 billion Egyptian Pounds must be injected in the railway sector to radically boost its performance. He further asserted that the government does not have the means to assume this cost. These statements were given in light of the latest train collision that occurred in late February 2018. Eventually, this debate around the benefits of involving the private sector culminated in the promulgation of Law 20/2018.

### **The Historical Background of Law 20/2018**

Law 20/2018 is the latest piece in a legislative sequence that began with Law 152 for the year 1980 which created ENR (“**ENR Law**”). According to the ENR Law, ENR is a national authority entrusted with the management of the railways’ utility. In the sense of Egyptian

administrative law, ENR is a typical public entity that assumes the management of a public utility which is directed towards serving the transportation needs of the greater public.

The ENR Law established a public monopoly. ENR was the sole entity permitted to construct, manage, operate, and maintain railway networks within Egyptian territory. This meant that ENR could not delegate to private contractors the performance of specific duties on its behalf under typical concession agreements. Article 2 of the ENR Law provided that:

*“The authority is competent – exclusively – to establish and operate railway networks on the national scale [...]”*

The ENR Law did anticipate the possibility of ENR incorporating joint ventures with third parties. However, the aim of such a vehicle would be to provide secondary support to ENR without prejudicing its statutory monopoly over the general management and operation of the national railway system.

In 2006, the ENR Law was first amended by virtue of Law 149 (“**Law 149/2006**”). Law 149/2006 represented a first step towards abrogating ENR’s monopoly. It was a significant development in that it permitted – for the first time – the cabinet to grant concessions to private entities unaffiliated to ENR. However, the subject matter of the concession related only to the “[...] establishment and operation of new railway networks [...]”. This meant that the existing network fell outside the scope of Law 149/2006. It also indicated that the role of the private sector was limited to the establishment and operation of these new networks, without extending this mandate to other aspects associated with the establishment and operation of railway networks. Law 149/2006 also did not repeal ENR’s monopoly under article 2 of the ENR Law. ENR remained the sole and exclusive entity authorized to operate and manage the railway network. The possibility to grant concessions was merely an exception to the general rule under said Article 2. Implicitly, Law 149/2006 reaffirmed the status quo.

### **Novelties under Law 20/2018**

Law 20/2018 differs fundamentally from Law 149/2006 in that it (i) has officially ended ENR’s monopoly, and (ii) adopts a concession-based system to engage private sector entities on a much broader scale. Article 2 of the ENR Law has been amended whereby reference to ENR’s “exclusive” competence has been omitted. Additionally, ENR is now authorized to grant concessions to private investors to “[...] *establish, manage, operate, or maintain all railway utilities* [...]”. Clearly, the wording has been expanded to capture all aspects of railway activities as well as all associated utilities. This reflects the State’s intention to ensure full involvement of the private sector in the rehabilitation of the railway sector.

### **Concessions under Law 20/2018**

The concession framework has been redesigned to streamline investments. Similar to Law 149/2006, ENR may grant concessions without having to observe a number of (outdated) special legislations related to concessions of public utilities. More interestingly, Law 20/2018 has also explicitly excluded the application of the Egyptian Tender Law. The latter represents the main legal framework that governs and regulates public procurement in Egypt. The

Tender Law, which is not designed for mega projects, has been blamed on several occasions before for slowing public procurement and paving the way for judicial challenges post-award.

Law 20/2018 has set-out the following guidelines:

- (a) The concessionaire must be selected through a transparent and competitive bidding process.
- (b) The concession period cannot exceed fifteen years (this is a constitutional requirement).
- (c) The concession agreement must regulate the supervision authorities of ENR to ensure uninterrupted operation of the railway network.
- (d) The Prime Minister, after securing the approval of the cabinet and based on the proposal of the Minister of Transport, is responsible for regulating all aspects of the concession. This includes formally issuing the concession, amending it, and determining (i) its terms and conditions, (ii) the Egyptian government's share of the proceeds, and (iii) the pricing mechanism.
- (e) The concessionaire may not assign the concession to another without obtaining the prior approval of the cabinet.
- (f) The concessionaire must maintain the assets in good working condition throughout the term of the concession. At the end of the concession's term, the concessionaire must transfer the assets to the State without any consideration. The assets should be in a usable state.

Law 20/2018 will be the main legal instrument that regulates the award of concessions. According to the above guidelines, the government appears to enjoy a wide discretion in electing the successful bidder and negotiating the terms of the concession.

### **Conclusion**

There is a general consensus that Law 20/2018 is necessary for the future of the Egyptian railway network, a vital public utility. According to official estimates, some 1.4 million passengers rely on the railway system daily.

However, concerns have been raised with respect to the effect of Law 20/2018 on the pricing of the service and the need for any private investor to recoup his costs and achieve a meaningful return on his investment during the (comparatively short) fifteen years' concession period.

Other concerns relate to the potential closure of passengers' lines that are deemed unprofitable.

It remains to be seen whether Law 20/2018 will be successful in channelling sufficient capital into a decaying railway network, and how the government will be able to strike the right balance between its dire need for private investment and considerations of public interest. Millions of common Egyptians rely on this utility for their daily transportation which puts the Egyptian government under tremendous pressure to deliver an affordable service. Practically,

this means that the possibility to increase fares may be restricted to a great extent. This may compromise the commercial value of the entire operation, especially given the relatively short timeframe of the concession.

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**If you would like more information about this topic then please contact us.**

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