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Israel's infrastructure boom

An unprecedented level of activity in transport, energy and defence is testing the skill sets of Israeli lawyers and attracting the interest of international firms

Israel is undergoing a massive transformation project to modernise its infrastructure. The government is thinking big. Ongoing initiatives include the Jerusalem Gateway, which will smooth the entrance into the city, and a mass transit system planned for Tel Aviv's metropolitan area.

The rise in projects means firms are eyeing profitable mandates by leveraging existing infrastructure client relationships and bidding as part of public tenders. However, the complex nature of this work and an unstable political ecosystem might test their lawyers.

Israel is in the midst of an infrastructure boom, with a series of projects involving fast trains, tunnels, new roads and metro systems in cities like Jerusalem and Tel Aviv. What are the main factors contributing to this spate of investments?

Mark Phillips, partner, Herzog Fox & Neeman: I think the government has realised that developing the country's transport infrastructure is critical – with house prices in the central areas rising and existing roads full to capacity, it knows the country needs efficient mass transit systems. So we are seeing light rail and metro projects being developed in Jerusalem, Tel Aviv and Haifa. We are also seeing efforts to reduce the use of private cars and to increase car occupancy by the use of carpool lanes on key roads, as well as discounts on tolls for vehicles with three or more passengers.

Jonathan Finklestone, partner, Meitar: For decades, Israel has suffered a severe deficit in infrastructure investment. Unlike other Western countries that have light rail or metro systems developed decades ago, Israel, as a relatively young country, has no such infrastructure stock. Therefore, even if the annual investment in infrastructure in Israel has been comparable to other countries, the starting point in terms of existing infrastructure has been significantly different.



Johnathan Finklestone

The Ministry of Finance has embarked on an ambitious programme for infrastructure investment using, in the main, the public-private-partnership (PPP) model, in order to bridge this gap. The ministry has also identified those areas where the PPP model is more appropriate and the needs are greatest. Therefore, the investment is being targeted at mass transit projects, in Tel Aviv, Jerusalem and Nazareth to Haifa, sea water desalination projects, renewable energy and waste-to-energy projects. The emphasis is on projects where the long-term benefits are higher, so less investment in highways and more investment in mass transit.

Shai Avnieli, partner, Barnea: Israel is in its biggest infrastructure boom. In addition to transport-oriented projects, there are huge investments in the following sectors: private energy production (green and traditional); infrastructure related to the recent natural gas find in Israel's waters; development of new air and sea ports; and the transfer of Israel Defence Forces' (IDF's) main army camps to southern Israel.

As for transport, Israel has been suffering, for a very long time, from a relatively old system. Owing to mainly political prioritisation, minister of transport was never considered a lucrative position – the issue was not promoted for decades. In 2009, Israel Katz started acting as the minister and held that position for more than a decade. While gaining considerable political power, he started promoting issues which were under his jurisdiction. That is why there has been so much progress in that area, which had culminated in the fast trains and metros being pushed forward with substantial force.

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Jonathan Finklestone, Meitar

The estimated cost of the shorter-term transport projects (Tel Aviv light railway Red, Green and Purple lines; Jerusalem light railway Green line; the fast lanes project, the Fast Railway Eastern Line) is around NIS35bn (£8bn). The longer projects (such as the metro system) are estimated at in excess of NIS100bn. As for the other areas, like energy, in July Israel decided to reform its energy sector, which included privatisation of existing power plants and the construction of new, privately owned power plants. This is the main reason for the rise in the construction of new power plants of various kinds.

In addition, for years the IDF was criticised for occupying very expensive real estate in Israel's already congested Tel Aviv metropolitan area. As a result, in 2015 the Israeli government decided on an initiative to transfer as many army camps as possible to the Negev, the desert

area in Southern Israel. Each transfer project is estimated in billions (the whole project has been budgeted at around NIS40bn).

What are the main projects that will be targeted by law firms? Are they mainly driven by public funds or private investors?

Finklestone, Meitar: As a firm, we have been involved in most of the large-scale projects in Israel. We are one of the go-to firms for complex projects. Our main focus is on pathfinder projects in which we are instrumental in developing precedent documents for such deals. For example, we have been involved in the first toll road, the first pumped storage project, the first wind project and the first solar projects. Given the range of projects in all sectors, the challenge will be to select those ones to which we can best apply our skill set.

Phillips, Herzog Fox & Neeman: Obviously, the light rail and metro projects are key targets for firms in Israel and abroad. These are big-ticket projects and there are multiple roles for law firms – government, equity, lenders and contractors – and in many cases these players will come from outside of Israel.

These projects are usually partly funded by the government in the form of a construction grant – the government may also perform part of the works itself to take certain risks away from the private sector. The remainder will be funded by the investors in the project and their lenders.

Avnieli, Barnea: Since infrastructure projects are complicated, with a multitude of players involved in it, every firm with an infrastructure practice will be involved. The question clients should ask themselves is which firm is best suited to which project.

With some firms boasting experience in the project finance side, some have better experience in accompanying lenders – which is more relevant to privately funded projects and less to publicly funded projects.

Others mainly focus on construction disputes, while only some can offer the combined expertise of their partners which makes them leaders in the infrastructure practice across all disciplines.

How are firms taking advantage of the situation? Are you boosting your infrastructure and projects practice to make the most of tenders?

Avnieli, Barnea: Providing legal advice to complex projects is not something just any lawyer can provide. This practice area is not some buzzword that lawyers can quickly adapt to and it is certainly impossible to quickly become adept in this field. Therefore, only a few law firms in Israel can really be 'part of the game'.

It should also be noted that conflicts of interests in this area are highly important to clients: we cannot, for example, represent governmental-owned entities and companies from the private sector at the same time.

Phillips, Herzog Fox & Neeman: There are actually not that many firms in Israel with real experience of complex project finance deals, so we are seeing more and more Israeli firms trying to break into this market.



Shai Avnieli, Barnea

We are also seeing a lot of interest from firms outside of Israel – mainly from the UK but also from the US. They understand that their clients – either developers or lenders – are looking at these projects, so they are preparing themselves by gaining more of an understanding of Israeli practise. We are definitely looking to grow our team by 'natural means' – training up lawyers from scratch.

Finklestone, Meitar: More firms are entering the infrastructure space, as more projects are published and the potential roles for law firms increases. We have one of the largest teams in Israel and we have a programme to increase the number of lawyers in our team.

What are the complexities related to infrastructure mandates in this scenario?

Phillips, Herzog Fox & Neeman: I think the biggest difficulty we have is explaining to international players that the risk allocation in Israeli projects is significantly different to the allocation in other countries.

There are some key issues which are flagged by every new company or lender entering the market as problematic and we have to try to help them understand the risk and how it can be dealt with – including by trying to convince the government to accept the need to make changes.

Generally, the government is not willing to change the allocation, so we have actually seen some companies pull out of the tender process because they could not get comfortable with these risks.

Finklestone, Meitar: The main challenge is that the projects are always more complicated than the clients envisage; nothing is ever plain vanilla or a cookie-cutter deal, even if the deal is in the same sector of a recently closed deal. Submission dates are often postponed and that impacts on fee arrangements and the staffing of deals. We are also instrumental in assisting our clients to bridge cultural, business and language barriers, in projects that by nature require large international consortia inside which Israeli and international companies must cooperate.

The main challenge is that the number of issues that may be encountered in a complex project can seem infinite and it is almost inevitable that an issue that no one initially considered becomes the issue that most time is spent upon.

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Avnieli, Barnea: The first complexity that I encounter as a lawyer is the fact that there is no good balance of power between the owners (who are mainly government entities) and the concessioners and contractors. Most of the contracts are aggressively drafted for the benefit of the state, and owing to a recent supreme court decision (*Bibi Roads v Israel Railroad*), there is a concern that contractual interpretation will lean even further towards the state.

This will result in concessioners either taking into account pessimistic scenarios, and as a result pricing themselves out of projects, or not taking those risks into account and face the consequences when they occur.

As a result, my view is that concessioners and contractors will have to handle themselves very carefully and accurately.

Will the outcome of the recent elections (Benjamin Netanyahu, Israel's longest-serving prime minister, has started talks to form a government after winning in Israel's third election within the same year, but was short of seats for a majority coalition) affect the projects?

Avnieli, Barnea: It is a very interesting question. It remains to be seen whether Israel Katz is going to stay as the minister of transport. If not, who will replace him? Will the ministry go back to being an unimportant one or will it continue to be a strong ministry? These questions, and other factors, are yet to be clarified. However, I am quite certain that at the least the projects which have already gone past the point of no return (in my estimation, around 35 per cent) will continue regardless of who will be the minister.

Phillips, Herzog Fox & Neeman: I think it is very unlikely that the elections will affect the projects since there seems to be a broad consensus that they are needed. The only possible issue could be a technical problem for budgeting new projects in the absence of a government and a state budget, but we are not quite there yet.

Finklestone, Meitar: It is unlikely that the elections will have an impact because there is across-the-board political consensus about the need for infrastructure investment and the professional civil service is managing the process in an efficient and responsible manner.

By **Cristiano Dalla Bona** 14 May 2020 09:30

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