

Private sector opportunities in the UAE water industry

Independent water projects on the increase in the UAE – new opportunities for developers and lenders.

Demand for water in the United Arab Emirates (UAE) continues to increase year-on-year with growth in population and industry straining existing water supplies. Following the International Water Summit hosted in the Emirate of Abu Dhabi in January 2016, the UAE underlined the growing importance of water security when it issued UAE Cabinet of Ministers Decision No. 7 of 2016, assigning specific water sector development competencies to the Ministry of Energy (MOE).

We anticipate increasing private sector participation in the development of the UAE water sector.

United Ventures & Investments Limited recently arranged a US\$150 million facility for Al Hamra Water Co. LLC to finance the development of a 22 MIGD desalination plant to be located in the Emirate of Ras Al Khaimah (RAK). And this week, the Federal Electricity and Water Authority (FEWA) reportedly prequalified bidders for a 45 MIGD desalination plant to be located in the Emirate of Umm Al Quwain.

These projects will be the first independent water projects (IWP) in the UAE, with Abu Dhabi's public-private partnership (PPP) utility projects to date all being cogeneration power and water production facilities, and are also very likely to be the first IWPs in the UAE to be entirely privately financed. FEWA's project will also be the first federally procured IWP in the UAE.

This *Client Alert* provides insight into the principal aspects of the regulatory framework governing private participation in the UAE water sector, which may be of interest to developers and lenders alike.

Federal Regulation

The UAE established the Ministry of Electricity and Water in 1972,¹ later merging it with the Ministry of Oil and Mineral Resources in 2004 to form the MOE.²

The MOE was restructured in 2014, and established two departments that oversee the water sector: the (i) electricity and desalinated water department, which primarily proposes policies and legislation relating to the desalinated water sector³; and (ii) regulation and control department, which, among other things, regulates and licenses desalinated water production and distribution facilities in those Emirates where FEWA provides water services^{4, 5}.

Although the MOE is a federal government entity, in practice its efforts are focused on assisting FEWA with developing water supplies in the Northern Emirates.

- *FEWA and the Private Sector*

The UAE established FEWA in 1999 primarily to provide electricity and water to the Northern Emirates and, when needed, to procure the development of power and water production facilities from the private sector.⁶

In April 2016, FEWA issued a request for a statement of qualifications (RFQ) for the development of a 45 MIGD seawater reverse osmosis (SWRO) in Umm Al Quwain.⁷ In August 2016, FEWA reportedly prequalified the bidders, and is expected to release the RFP in early September 2016. This is the first IWP that FEWA will procure, and is reportedly intended to supply water not only to Umm Al Quwain, but also some of the other Northern Emirates. The project will be one of the first IWPs in the UAE, with Abu Dhabi's PPP utility projects to date all being cogeneration power and water facilities.

FEWA will likely look to replicate the success of the IWPP programs that the Abu Dhabi Water and Electricity Authority (ADWEA) and Dubai Electricity and Water Authority (DEWA) implemented in Abu Dhabi, Dubai and Fujairah.

ADWEA and DEWA projects typically permit, under the terms of the procurement process, private sector participants to own up to 40% of the project company; however, the successful bidder on FEWA's project will reportedly be able to own 100%. Nevertheless, until such time as the UAE government might relax the legal requirement for 51% UAE ownership in all UAE companies, bidders will need to partner with a UAE person to comply with the 51% national ownership rule (effectively limiting the successful bidder's direct shareholding to 49%).⁸

- *Licensing and federal support*

Of interest will be the terms of the license for the project, which the MOE (as FEWA's regulator) will presumably issue, and whether the MOE or another federal government entity will provide any support (financial or otherwise) for the project in a manner similar to that of ADWEA and DEWA for their own Emirate-level projects (see below).

Emirate Regulation

Abu Dhabi

Abu Dhabi established its own water and electricity authority (ADWEA) and its own regulation and supervision bureau (AD-RSB) in 1998 under Abu Dhabi Law No. (2) of 1998.

- *ADWEA and the Private Sector*

ADWEA's primary responsibility is to develop power and water supplies for the Emirate of Abu Dhabi. All new water production capacity should, insofar as possible, be designed, built, financed, owned and operated through the utilization of private sector funds (whether domestic or foreign).⁹

ADWEA provides support for independent water and power projects in three key ways: ADWEA (i) can enter into binding commitments with the private sector regarding the funding of public sector participation in such projects (including providing support for ADWEC's payment obligations under any water purchase agreement); (ii) leases or procures the lease of land the Government of Abu Dhabi owns, for the implementation of such projects and related usage rights; and (iii) provides assistance (including liaising with governmental authorities) with the procurement of governmental consents and permits required for implementing such projects.¹⁰

The private sector (both domestic and foreign) is specifically permitted to: (i) purchase and own shares in any entity (including water producers) ADWEA establishes; and (ii) participate in the management of the business and affairs of any entity.¹¹

- *AD-RSB*

AD-RSB has the sole and exclusive authority to regulate the water sector in Abu Dhabi, and has full power to regulate all licensed operators economically and technically in accordance with the law.¹² AD-RSB also has the exclusive right and power to license any person to conduct any regulated water activity such as the desalination of water; the transmission of water by trunk mains pipeline; the distribution of water by mains pipeline; supply of water to premises; storage of water; and supply of water by an unlicensed operator to the connection grid of a licensed transmission operator.¹³

- *Licensing*

No person may conduct regulated water activities unless licensed to do so or that person is exempt from being so licensed.¹⁴

To date the only exempted water activities are small-scale desalination of water up to 2 million litres/day per facility or less than 10 million litres/day of aggregate net declared capacity, provided the supply and distribution of water output is captive and non-commercial.¹⁵

Water desalination and storage licenses are typically issued for the duration of the water purchase agreement with ADWEC, subject to early termination and revocation (e.g., due to a breach of the conditions of the license, insolvency or a change in control).

The licenses typically contain a series of conditions, which, among other things, prohibit the licensee from: (i) purchasing or otherwise acquiring water for the purpose of sale to third parties; (ii) transmitting water except as necessary to deliver water into the transmission system; (iii) engaging in the business of water storage except for operational balancing; (iv) engaging in the distribution or supply of water to any premises; (v) desalinating water in excess of the expressly authorized capacity; and (vi) unless permitted by the AD-RSB, holding any economic interest in entities which, either individually or in partnership with other entities, provide more than a specified percentage of the water production capacity of desalination facilities in Abu Dhabi.¹⁶

- *Sale of Water/Single-Buyer Market*

Licensees cannot, unless exempted, sell water production capacity or output to any person or entity other than the Abu Dhabi Water and Electricity Company.¹⁷

- *Financing related consent*

AD-RSB consent is also required for the creation and maintenance of security interests in a licensee's assets as may be required for any financing of independent water and power projects.¹⁸

- *Asset disposals and subcontracting*

More recently, the license issued to Mirfa International Power and Water Company in October 2014 introduced a new condition effectively requiring RBS consent before undertaking any asset disposals (i.e., any sale, gift, license, loan, mortgage, charge or grant of any other encumbrance, or the permitting of an

encumbrance to subsist or any other disposition to a third party) and/or relinquishing operational control (*i.e.*, subcontracting any substantial part of the responsibility for the performance of the licensed activity).¹⁹ This is the first license to contain such conditions the AD-RSB has issued.

- *License transfers*

Licenses are non-transferable unless they expressly permit a transfer. Permitted transfers are subject to obtaining the prior written consent of the AD-RSB and such other conditions as the AD-RSB may stipulate in the license.²⁰

Copies of the licenses currently in issue to producers (utility and small scale as well as self-regulators), transmission and distribution companies, as well as the “single-buyer” ADWEC, may be found on the AD-RSB public register.²¹

Ajman, Fujairah and Umm Al Quwain

Ajman, Fujairah and Umm Al Quwain do not have their own electricity and water authority, and rely on FEWA (and ADWEA in the case of Fujairah) for their water needs. See the earlier paragraph on Federal Regulation for FEWA’s current project in Umm Al Quwain.

Dubai

Dubai established its own electricity and water authority (DEWA) in 1992 under Emiri Decree No. (1) of 1992, and its own regulation and supervision bureau (DB-RSB) under Executive Council Decision No. (2) of 2010.

- *DEWA and the Private Sector*

DEWA’s primary responsibility regarding the water sector is to develop, own, operate and maintain water desalination plants and water distribution networks in the Emirate of Dubai.²²

To support those responsibilities, DEWA is authorized to purchase water from third parties; develop water desalination plants solely or in partnership with third parties; purchase and sell fuel to those entities licensed to produce water; invest and borrow funds with or without guarantee (subject to the Ruler’s prior approval); and grant usufruct or other rights relating to land associated with water production facilities.²³

- *DB-RSB*

DB-RSB is authorized to regulate the water sector in the Emirate of Dubai, and license all participants in that sector.²⁴ DB-RSB is the only entity that can license persons to conduct regulated water activities such as desalination and supply to DEWA.²⁵

- *Licensing*

No person or entity (public or private) may conduct regulated water activities unless licensed to do so. The only exception to this is DEWA, being the only entity legally authorized to develop water production in the Emirate of Dubai.²⁶

- *Sale of Water/Single-Buyer Market*

No person or entity (public or private) may sell, supply or provide water production to any person, inside or outside of the Emirate of Dubai, other than DEWA.²⁷

- *Asset disposals and subcontracting*

Licensees may not dispose (*i.e.*, sell or transfer title, lease, grant any security interests, create or waive any real rights) of their main assets without the prior written approval of the DB-RSB.²⁸

Generally, licensees may not enter into any subcontract with any entity to conduct regulated water activities unless the subcontract is disclosed at the time of the license application. However, if licensees wish to enter into such a subcontract after the license is issued, they must obtain the prior written approval of the DB-RSB.²⁹

- *Financing related consent*

As an exception to the above restrictions on asset disposals, the DB-RSB can approve the grant of any security interest over a licensee's main assets to the extent required to facilitate the financing of water production facilities.³⁰

- *License transfers*

Licenses may not be transferred without the prior written consent of the DB-RSB.³¹

- *Applicable law and dispute resolution*

Licensees and third parties are free to designate the governing law and dispute resolution procedures in contracts related to regulated water activities. The laws of the Emirate of Dubai must, however, govern any contracts between licensees and DEWA and disputes must be finally resolved pursuant to Dubai-based arbitration under the rules of the Dubai International Arbitration Centre.³²

Copies of the licenses currently in issue to producers can be found on the DB-RSB public register.³³

Ras Al Khaimah

RAK established its own electricity and water authority (RAKEWA) in 2013 under Emiri Decree No. (4) of 2013. RAKEWA's primary objectives are two-fold. First, to regulate the ownership, management, operation and maintenance of water desalination plants, water fields, water distribution networks and other assets and facilities related to the water sector in RAK. Second, to monitor the prices of water sold to consumers in RAK to ensure fairness and transparency.

As of the date of this alert, we understand that RAKEWA is not in operation and the Ras Al Khaimah Investment Authority (RAKIA), the Ras Al Khaimah Department of Economic Development (RAKDED) and the Environment Protection & Development Authority (EPDA), for the time being, regulate desalination activities. RAKIA, RAKDED and EPDA respectively issue industrial and commercial licenses and environmental permits to commercial companies, such as Al Hamra Water Co., undertaking water desalination, refining and distribution activities.

FEWA has traditionally been the dominant player in most of the Northern Emirates — Ajman, Fujairah, Ras Al Khaimah, Sharjah and Umm Al Quwain — so the fact that the Emirate of Ras Al Khaimah has enabled the introduction of a fully private and independent water producer such as Al Hamra Water Co is a welcome development.

Sharjah

Sharjah established its own electricity and water authority (SEWA) in 1995 under Emiri Decree No. 1 of 1995. SEWA is authorized to own, manage, operate and maintain water desalination plants, water wells, water networks and related assets,³⁴ and to contract with third parties to assist SEWA in fulfilling its objectives.³⁵ SEWA is also authorized to determine the price of water and water connection fees (subject to approval from the Sharjah Executive Council).³⁶

Conclusion

The success of the Al Hamra and FEWA IWPs in the Emirates of Ras Al Khaimah and Umm Al Quwain should pave the way for further opportunities for the private sector to meet the continually growing demand for water in the UAE.

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Please note this alert is based upon publicly available English translations of Arabic laws, and readers should be aware that the Arabic version of those laws is the prevailing version.

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Endnotes

- ¹ Art. 17 of Federal Decree No. 1 of 1972 (Establishing the Competencies of the Ministries and Powers of the Ministers).
- ² Art. 1(2) of Federal Decree Law No. 3 of 2004 (Merger of Competencies of Ministries).
- ³ Art. 23(1) of UAE Cabinet Decision No. 23 of 2014 (Organizational Structure of the Ministry of Energy).
- ⁴ Art. 26(1) and (4) of UAE Cabinet Decision No. 23 of 2014 (Organizational Structure of the Ministry of Energy).
- ⁵ <https://www.moenr.gov.ae/en/about-ministry/organizational-chart.aspx#page=1>
- ⁶ Arts. 3(1) and 23 of UAE Federal Law No. 31 of 1999 (Establishment of the Federal Electricity and Water Authority).
- ⁷ <http://www.fewa.gov.ae/en/TenderAndRegistration/Pages/EOI-Invitation.aspx>
- ⁸ Art. 10 of Federal Law No. 2 of 2015 (Concerning Commercial Companies).
- ⁹ Art. 34(2) and 131 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹⁰ Arts. 11 and 132 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹¹ Art. 148 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹² Art. 48 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹³ Arts. 82 and 71(1) and (5)-(9) of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹⁴ Art. 72 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹⁵ Electricity and Water (Licence Exemption) Order No. 1 of 2012 issued by the Abu Dhabi Regulation & Supervision Bureau.
- ¹⁶ Arts. 89, 90 and 92 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹⁷ Art. 74 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹⁸ Art. 133 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ¹⁹ Condition 3 – Asset Disposal of the Mirfa International Power and Water Company Water Desalination and Electricity Generation Licence.
- ²⁰ Art. 126 of Abu Dhabi Law No. 2 of 1998 (Concerning the Regulation of the Water and Electricity Sector in the Emirate of Abu Dhabi).
- ²¹ <http://rsb.gov.ae/en/sector/licence-holders>
- ²² Art. 3(a)(i) of Dubai Emiri Decree No. 1 of 1992 (Establishing the Dubai Electricity and Water Authority).
- ²³ Arts. 3(b) and 6(g) of Dubai Emiri Decree No. 1 of 1992 (Establishing the Dubai Electricity and Water Authority) and Art. 9 of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).
- ²⁴ Art. 2 of Dubai Executive Council Decision No. 2 of 2010 (Establishing an Office for the Regulation and Control of the Electricity and Water Sector in the Emirate of Dubai).
- ²⁵ Art. 10 of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).
- ²⁶ Art. 5 of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).
- ²⁷ Arts. 5 and 23 of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).
- ²⁸ Art. 22 of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).
- ²⁹ Art. 17 of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).
- ³⁰ Art. 22(b) of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).
- ³¹ Art. 21(a) of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).

³² Art. 24 of Dubai Law No. 6 of 2011 (Regulating the Participation of the Private Sector in Electricity and Water Production in the Emirate of Dubai).

³³ <http://www.rsbudubai.gov.ae/resources/licences/>

³⁴ Art. 5(2) of Sharjah Emiri Decree No. 1 of 1995 (Establishment of the Sharjah Electricity and Water Authority).

³⁵ Art. 5(7-c) of Sharjah Emiri Decree No. 1 of 1995 (Establishment of the Sharjah Electricity and Water Authority).

³⁶ Art. 7(6) of Sharjah Emiri Decree No. 1 of 1995 (Establishment of the Sharjah Electricity and Water Authority).