

Reforms in Road Financing Policies

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Abstract:

The purpose of this presentation/ abstract is to have one insight on reforms which are needed in Roads projects based on real cases.

Consulting engineering companies and Employers are facing issues during Procurement stage for works in Public Sector financed by international institutions (World Bank, ADB, EU, EBRD....).

The procurement stage is important and it should be efficient and accurate in order to avoid further claims/disputes from the Contractor. Most of the Contractor's claims find their roots in issues not defined at all or poorly defined during this stage or in Design.

Reforms in road financing policies are needed especially in Procurement stage where the common issues are presented below (non-exhaustive list of issues):

1. Strategy selection : prequalification / postqualification criteria
2. Risk mitigation
3. Forms of Contract
4. Accurate Data
5. Rushed tendering stage
6. Abnormally low tender
7. Tenders exceeding Client's cost estimate
8. No offer(s) received from the tenderers
9. No responsive offers
10. Fraudulent practice

Supports, precise and robust rules from the financial institutions are needed. The more safeguard is in place and enforceable, the less of an affect those issues will have on the projects.

1 - Background

Experience has shown that Clients need to improve their skills in the fields of Design and Procurement. A cultural change is also needed to award contracts on the basis of fair competition and the merits of the successful Contractor, in order to ensure that maximum value for public money is achieved.

Since most of procurement issues can be identified at an early stage, they can reasonably be resolved fairly and easily. It is obvious that support, and precise and robust rules are required from the financial institutions. The more safeguard is in place and in force, the less those issues will affect the Roads projects.

It is worth noting that the World Bank and other financial institutions have made significant progress in the evolution of procurement throughout the world. Despite those positive steps, the financial institutions encounter difficulties with the use of national procurement systems⁽¹⁾.

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2 - Organization of Procurement in Public Sector

Under the Loan Agreements and other agreements signed between a Client and a financing institution for the purpose of implementation of a project, the Client is mostly obliged to establish a Project Implementation Unit (PIU), adequately staffed and financed for management of the implementation of the respective Project, including management of the Project accounts and reporting on Project implementation.

The PIU may be responsible for the following tasks (list non-exhaustive) :

- Development, review and implementation of project management procedures, standards and practices for efficient Project implementation.
- Managing resources across all projects administered by the PIU.
- Establishment and maintenance of Project management tools and techniques, and support for the project managers in the use thereof.
- Organization and management of project management training for all appropriate staff members.
- Performing duties related to planning, scheduling, risk management, scope management, financial management, status reporting, and other project management activities.

Regarding procurement of goods, works and services, the PIU is usually responsible to (list non-exhaustive):

- prepare and implement the Project procurement plan for goods, works and services, and conduct required tenders based on the Banks' procurement rules and policies;
- prepare tender documents for procurement of goods, works and services based on technical specifications and terms of reference, in accordance with the Project procurement plan;
- establish and ensure efficient work of the tender committee to procure goods, works and services under the Project;
- ensure compliance of tender procedures with the requirements of the Banks as regards transparency, equal treatment of participants, non-discrimination:
 - prepare tender documents;
 - hold tender opening sessions;
 - provide clarifications concerning tender documents;
 - prepare draft evaluation reports;
 - obtain the Banks' nonobjection on the evaluation reports;
- prepare draft contracts with suppliers of goods, works and services in accordance with the Banks' requirements and standards.

In view of the foregoing, the financial institutions should primarily ensure that a clear, robust and efficient set of procurement procedures is in place, and the requirements of the Loan Agreement and other Project Agreements are respected.

Once the PIU is formed and the procedures are established, the Client should decide on the procurement strategy; simply said, the Client should define well the "product" he prefers. Feasibility studies and/or Designs or Employer's Requirements are a good tool in the road construction industry, incorporating location, technical standards, work programs, time constraints, etc.

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Once the feasibility study or Employer's Requirements have been prepared, the Client should be in position to choose the best procurement and contractual strategy.

A few basic questions should be answered:

- Allocation of functions: Who will be responsible for the design?
- Allocation of risks: Who bears the risks of unforeseen events?
- Payment: is it a lump sum or a measurement contract?
- Resolution of conflicts: is it through dispute board or any other mechanism?

The success of a Road projects is essential and possible; a good contractual strategy and fair type of contract are the keys to such success.

3 - FIDIC Conditions of Contracts for Works

FIDIC (Fédération Internationale des Ingénieurs Conseil) was founded in 1913 by associations located in 3 French-speaking countries – Belgium, France, and Switzerland.

In 1999, FIDIC published 4 different Contracts for almost all types of works:

- Conditions of Contract for Works designed by the Employer (Red Book)
- Conditions of Contract for Works designed by the Contractor (Yellow Book)
- Conditions of Contract for EPC – Engineering, Procurement and Construction (Silver Book)
- Conditions of Contract for small Works (Green Book)

These Conditions of Contract have been considered complete and fair by most of the professionals in Construction Industry. Also, it is worth mentioning that they have been considered equitable and flexible.

Since 1999, a few MDBs (Multilateral Development Banks) have adopted FIDIC forms of Contracts as part of their Standard Bidding Documents, and have been requiring that the Borrowers follow them.

In May 2005, FIDIC published the first MDB harmonized edition also called the Pink Book. Those are Conditions of Contract for Works designed by the Employer, similar to the Red Book 1999 edition. In March 2006, FIDIC made a few adjustments of the General Conditions.

In June 2010, FIDIC published a revised edition with the support of the following participating Banks:

- African Development Bank Group (ADBg)
- Asian Development Bank (ADB)
- Black Sea Trade and Development Bank
- Caribbean Development Bank
- Council of Europe Development Bank
- European Bank for Reconstruction and Development (EBRD)
- Inter-American Development Bank
- International Bank for Reconstruction and Development (The World Bank)

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Nowadays, most of the Tender/Bidding Documents for the Procurement of Road Works in the international competitive environment include FIDIC forms of Contracts. Most of the Borrowers who apply for financing from the above banks are aware of those conditions of contracts, but there is still a lack of training in some countries, such as Bhutan, Mozambique, Ukraine,

4 - The 10 Common Issues in Procurement

In order to present the 10 common issues in Procurement, the Author demonstrates a few cases from Central America, Asia and Europe to highlight the specific issue. For confidentiality reasons, it may happen that relevant information may not be provided.

The following is a non-exhaustive list of issues to be explained:

1. Strategy selection: pre-qualification / post-qualification criteria

MDBs such as EBRD, EIB, ADB and others financial institutions have adopted pre-qualification criteria. This is a preliminary stage in a bidding/tendering process when it is determined if the bidder/tenderer has the requisite resources and experience to complete the job as required by the Client. The bidder/tenderer will be required to demonstrate their capacity to perform the works or services of a particular type by giving evidence of their (list non-exhaustive):

- experience in similar works;
- history of non-performance;
- history of litigation;
- financial situation.

Some Clients opt for post-qualification criteria, i.e. when a procedure is settled after qualification has been awarded. Significant drawbacks have been analyzed by the financial institutions and recorded for the Clients' benefits. Among such drawbacks, a detailed plan on how the entire process will run is needed. National laws and regulations may have no specific legal interpretation of what is or is not permitted; thus, a careful consideration of the legal boundaries is necessary ⁽²⁾.

In light of the above, the Author's opinion is that the Banks should continue with pre-qualification criteria. In case of large-scale work contracts, two-stage bidding/tendering (as explained in Sub-chapter 6 "Abnormally low tender") should be adopted by the Clients.

2. Risk mitigation

It is important for the Clients to make a risk analysis of their road project(s) during the tender stage. Once this is done, they will be able to identify, evaluate and treat the risk(s). Secondly, it may happen that there are some incompatibilities between the Financing Bank's and the

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Client's procurement strategies. Financing institutions may encounter difficulties with the national procurement system in place.

In many cases, the Author has evidenced that risk procedures and risk register have not been implemented by the Clients before launching the tenders. Risk assessment of a Project is a task which requires attention, professionalism and experience. Obviously, if such practice was more common, many claims from the Contractors could have been avoided.

During the construction stage, it appears that risk management is a practice in some countries. In the Qatari road project, Expressways group 8a P007, a risk review workshop is held every two weeks by the Consultant in order to evaluate the risks of the project completion and to formulate mitigation measures. Risks are identified, evaluated and classified in different groups such permits, approvals, data information, design, land – site availability, interface with third party, public relations, changes in regulations and tax policy and site conditions.

As all parties agreed with the approach, this road project had good results in terms of risk mitigation.

In view of the foregoing, the Author's opinion is that the Banks should not finance a Client's project unless a clear and robust risk assessment of the project has been done. During the construction stage, the Financing Banks should also check that the Contractor's and Client's representatives have their own procedures in terms of risks mitigation.

3. Unbalanced and unfair conditions of contract

A case in Jamaica has been used for explaining the risks for the parties having unbalanced and unfair conditions of contract.

Located in Jamaica, the Works Contract covers the infrastructures in the Kingston Port, including:

- Refurbishment of 1,218m berth on Southern Quays to accommodate 14,400 TEU vessels with 14.7 ml vessel draft. The refurbished berth has future capacity to accommodate vessels up to 15.5 ml draft.
- Dredging works: deepening, realignment of the nautical accesses, as well as upgrade of navigation aids, to accommodate 14,400 TEU vessels with 14.7 ml vessel draft.
- Yard's pavement rehabilitation.

The contract is based on the EPC FIDIC Book 1999 and the English governing law.

The contract has been awarded for a total amount of 130 millions of euros ⁽³⁾.

During the procurement stage, the bidders/tenderers have raised several issues:

- The Contract Agreement incorporating FIDIC backbone amended with Concession Agreement induces a high contract management complexity. The main issue is that many parties, i.e. Lenders, Lender Technical Advisor, Independent Engineer, Employer's Representatives may have interferences or interfaces. The back-to-back principle remains applicable for the EPC Contractor.

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- The Contractor shall have no claim (neither time extension nor compensation for additional costs) and will not benefit from a back-to-back claim in this respect for the dredging works except for sections n°4 and n°5, only if physical conditions differ from Geotechnical Baseline Report, and this results in delays, to an extension of time within the maximum limit of 3 months. No entitlement to compensation for additional costs.
- The overall Contractor's responsibility provides that the EPC Contractor is responsible for errors in the Employer's Requirements and unforeseen difficulties.
- The fit-for-purpose obligation under the English law has an impact of high risks related to performance securities.

The aggregate cap on liability is set at 100% of the Contract Price.

In light of the above, the Author's opinion is that the EPC Contracts have a few unbalanced and unfair conditions which have been considered as having an "unacceptable risk allocation"⁽⁴⁾. As a conclusion, it is important to have balanced and fair conditions of contract. It would be convenient if the Financing Banks involved technical experts during tender preparation in order to avoid further Contractor's claims/disputes during execution of works.

4. Inaccurate data during tender stage

A case in Romania has been used for explaining the consequences of having inaccurate data during the tender stage.

Located in the eastern part of western Romania, the Arad bypass, an urban motorway of 12.250 km is part of the pan-European corridor IV. The motorway is situated inside and outside the built-up area of Arad City. The Arad Bypass Contract is based on the Design & Built FIDIC Book 1999 and the Romanian governing law.

The Project has been financed by the European Investment Bank (EIB), EU and Romanian funds; the contract has been awarded for a total amount of 428,895,737.20 RON (contractual exchange rate: 1 EUR = 3.5555 RON). During the construction of the Project, the Contractor claimed for errors and inaccurate data in the Employer's requirements.



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Most of the Contractor's claims resulted from:

- Employer's delay in providing right of access and land acquisition;
- Employer's failure to localize an electricity pole belonging to a high-voltage network (110 kV);
- Employer's failure to identify an airport landing light system;
- inaccurate data regarding level of extraordinary waters (NAE) for the Mures river;
- unclear information regarding noise protection barriers;
- missing documents and approvals from authorities.

Based on the above case, it is important to have accurate data during the tender stage. It would be convenient if the Financing Banks involved technical experts during the tender preparation, in order to avoid potential costly Contractor's claims.

5. Rushed tendering stage

In international competitive environment, the tendering /bidding documents are usually prepared in 3 parts, as follows:

- Tendering/bidding procedures: This part specifies the procedures that tenderers/bidders should follow when preparing and submitting their tenders/bids. Procedures for submission, opening, technical and financial evaluation of tenders/bids, and for the award of contract.
- Requirements: This part contains technical specifications, drawings, schedules of prices or bills of quantities, personnel and equipment requirements.
- Conditions of Contract and Contract Forms: This part contains the General Conditions and Particular Conditions which govern the Contract between the successful tenderer/bidder (the Contractor) and the Client (the Employer).

The part requiring most attention and professionalism is the requirements which are usually prepared by the Client or their consultant.

During the assessment of the Contractors' claims, the Author received from the latter numerous comments regarding the quality of the tender/bidding documents. Unfortunately, many Clients are unwilling to invest in preparing this documentation.

In the past, the Clients would spend years to prepare good, clear and robust requirements, but nowadays they want perfect requirements in a few months, and an accurate cost estimate soonest. Due to the rush and time pressure, the tenders are not prepared with good quality, and numerous amendments are issued during the tender/bid stage.

Based on the aforesaid, the Author's opinion is that the Financing Banks should warn the Clients much more to prepare good tender/bid requirements in order to avoid Contractor's claims and disputes.

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6. Abnormally low tender

A case in Ukraine has been used for explaining abnormally low tender.

Located in the eastern part of Ukraine, the Dnipro metro project aims to complete the 4 km extension for the existing metro within 5 years ⁽⁵⁾.

The Client adopted the following two-stage tender for this large-scale project:

(a) The first stage tender consisted of a technical proposal only, without any reference to prices, and a list of any deviations to the technical and commercial conditions set forth in the tender documents or any alternative technical solutions a tenderer wishes to offer, and a justification therefore, provided always that such deviations or alternative solutions do not change the basic objectives of the project. Following evaluation of the first stage tenders, the Client invited each tenderer meeting the qualification criteria and having submitted a technically responsive tender to a clarification meeting. Only qualified tenderers submitting a technically responsive and acceptable first stage tender have been invited to submit a second stage tender. The first stage of the tender was launched in early 2013, and eight proposals were submitted to the Client in July 2013.

(b) The second stage tender consisted of an updated technical tender incorporating all changes required by the Client as recorded in the Memorandum to the clarification meeting or as necessary to reflect any amendments to the tender documents issued subsequent to submission of the first stage tender, and the commercial tender. The second stage of the tender was launched in late 2014.

Due to financial, economic, social difficulties, and war in the eastern part of Ukraine, only 4 tenderers from Italy, China, Turkey and Ukraine submitted their offers in October 2015.

The following tender prices were submitted for the second stage tender evaluation:

Tenderer A : EUR 323.865.682, inclusive of VAT / EUR 269.888.068,00, exclusive of VAT

Tenderer B : EUR 297.319.328, inclusive of VAT / EUR 247.766.106,86, exclusive of VAT

Tenderer C : EUR 338.602.876, inclusive of VAT / EUR 282.169.063,10, exclusive of VAT

Tenderer D : EUR 224.000.000, inclusive of VAT / EUR 186.666.666,67, exclusive of VAT

The first Employer's cost estimate established during the feasibility study comprised EUR 301 Million, exclusive of VAT, in 2011.

Tender D was considered as "abnormally low" by the Client who analyzed his risks, including reduction of progress of works or suspension or termination of contract resolved through international arbitration. After long discussions, it was decided to increase the Performance Security.

In July 2016, the World Bank published a guide to the identification and treatment of abnormally low bids and proposals.

However, the Author's opinion is that other MDBs should urgently develop a clear and robust procedure and mechanism facilitating rejection of abnormally low tenders under certain circumstances.

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If the above is unacceptable, the Banks could develop an appropriate procedure to address abnormally low tenders through the tender evaluation process.

7. Tenders exceeding Client's cost estimate

A case in Bhutan has been used to explain the difficulties of having bids/tenders exceeding the Client's cost estimate.

Phuentsholing, a town in the southern part of Bhutan, is the principal commercial hub for all kinds of business, almost 90% of import and export of the country is done from this place. It is also called "the gate of Buthan". In order to improve it and to ease customs problems, the Client decided to build a mini dry port for customs clearance of import and export traffic, storage, transshipment, etc. ...

The project is financed by the ADB, and the procurement norms followed are single-stage two-envelope. Only three bidders/tenderers participated in the bid. During the opening, out of the three bidders/tenderers, one was rejected for not containing the technical proposal.

While evaluating the technical proposals, one bidder/tenderer was found to have no experience in designing. Since the project was based on the Design and Build concept, the bidder/tenderer was disqualified on this ground.

The last bidder/tenderer was found substantially compliant during the evaluation, and the technical bid evaluation report was sent to the ADB for their information and concurrence.

After receiving the concurrence from the ADB, the financial bid was opened in the presence of the bidder/tenderer. The quoted amount was 65% above the Client's cost estimate.

The tender committee felt the quote was too high and far from the available budget. After a long discussion, it was decided to commence negotiations. A date was fixed, and the bidder/tenderer was requested in writing to attend the negotiation meeting. During the negotiation meeting, the bidder/tenderer was asked to reduce his bid price. After a long discussion, the bidder/tenderer asked for some time to review his earlier estimate and to come up with new quote.

After five days, the bidder/tenderer submitted his new bid price which was still 28% above the Client's cost estimate. The bid price, though, was accepted by the tender committee on condition that the ADB accept it too. The contract was finally awarded to the successful bidder/tenderer.

In view of the foregoing, the Author's opinion is that the Financing Banks should continue to support the Clients having understanding and flexibility whenever it is needed, in order to avoid re-tendering and losing time and cost.

8. No offers received from tenderers

The Author has never faced the case when the Client and/or his consultant(s) have received no proposals from the tenderers/bidders during the tender stage.

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This usually happens when the Client and/or their consultant(s) imposes high requirements in terms of financial resources, annual turnover and construction experience.

As Advisor to Clients, the Author always recommended them to analyze the local and regional market in order to fit the reality adequately.

In light of the above, the Author's opinion is that the Financing Banks should continue to support the Clients helping them to prepare good analysis in order to avoid the nightmare of receiving not a single proposal on the day of tender/bid opening.

9. No responsive offers

A non-responsive offer is usually rejected if there is evidence of a nonconformance, such as:

- tender/bid valid for a shorter period;
- tender/bid not accompanied with a substantially compliant bid security or bid-securing declaration.

According to the ADB Standard Bidding Documents / Section 1 - Instructions to Bidders / Art. 30.2,

‘‘A substantially responsive Technical Bid is one that meets the requirements of the Bidding Document without material deviation, reservation, or omission’’.

The tenderer/bidder should be aware of the nonconformance criteria before submitting their offer.

Non-responsive offer is a cause for concern of the Clients and their consultants if there is only one offer received. In such cases, the tender should be cancelled, and a new tender should be launched.

As Advisor to Clients, the Author always recommended them to make clear the nonconformance which will be subject to rejection before tender/bid submission.

Other criteria defined by the ADB, ADBG and EBRD for rejection of tender/bid are as follows:

- failure to furnish all information or documentation required by the tender/bid documents;
- any attempt by a tenderer/bidder to influence improperly the Employer in the evaluation of the bids or contract award decisions;
- failure of the tenderer/bidder to comply with the request to submit the necessary information or documentation, within a reasonable period of time;
- absence of the total bid price in the Letter of Price Bid.

In view of the foregoing, the Author's opinion is that the Financing Banks should define reasonable nonconformance criteria in respect of non-responsive tenders/bids that have to be rejected.

10. Fraudulent practices

Unfortunately, fraudulent practices still occur nowadays in road construction industry ⁽⁶⁾.

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It is also the view of the Author that Reforms in Road Financing Policies are needed in terms of fraud and corruption in order to observe the highest standard of ethics during the procurement and execution of the contracts. In the countries where cases of fraud and corruption have been evidenced, the MDBs should not finance projects where the Clients have been involved in the illegal practices.

The Financing Banks should be more active in auditing the projects, including turning the sites, checking correspondence, variations, fake Contractor's claims, etc.

The Borrowers should have strong anticorruption and sanctions policies. Some countries in Africa (Benin, Rwanda,) have made significant efforts in this regard.

FIDIC should also urgently change Sub-Clause 15.6 of the Harmonized Edition which says:

“If the Employer determines, based on reasonable evidence, that the Contractor has engaged in corrupt, fraudulent, collusive or coercive practices, in competing for or in executing the contract, then the Employer may, after giving 14 days notice to the Contractor, terminate the Contract and expel him from the Site, and the provisions of Clause 15 shall apply as if such termination had been made under Sub-Clause 15.2 [*Termination by Employer*].

Should any employee of the Contractor be determined, based on reasonable evidence, to have engaged in corrupt, fraudulent or coercive practice during the execution of the work then that employee shall be removed in accordance with Sub-Clause 6.9 [*Contractor's Personnel*].

[*For contracts financed by the Asian Development Bank:*]

For the purposes of this Sub-Clause:

- (a) “corrupt practice” means the offering, giving, receiving, or soliciting, directly or indirectly, anything of value to influence improperly the actions of another party;
- (b) “fraudulent practice” means any act or omission, including a misrepresentation, that knowingly or recklessly misleads, or attempts to mislead, a party to obtain a financial or other benefit or to avoid an obligation;
- (c) “coercive practice” means impairing or harming, or threatening to impair or harm, directly or indirectly, any party or the property of the party to influence improperly the actions of a party;
- (d) “collusive practice” means an arrangement between two or more parties designed to achieve an improper purpose, including influencing improperly the actions of another party”.

The lack of reciprocity for Contractors is obvious in this sub-clause, and it can be abused by dishonest Employers.

5 - Next Challenges for Financial Institutions

Firstly, it is worth noting that most of the financial institutions do not have precise rules and guidance to face some common procurement issues in public sector. However, the World Bank launched on 01/07/2016 twenty-three new standard bidding documents to reflect the new framework to operationalize the regulations in terms of request for proposal, abnormally low tenders, negotiations, etc. Other MDBs have not yet followed the same improvement way.

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The financial institutions should make sure that the consulting engineers drafting tenders and contracts are focused on key points such as technical aspects (sub-soil conditions, survey reference points, design accuracy, ...), design responsibility allocation depending on GCC, procurement aspects (site visit to be well organized, contract documentation to be cross-checked, legal review, etc.).

Regarding more transparency during the procurement stage, it is very much welcome that the EBRD supports Ukrainians in ‘‘a new era of transparency after decades of endemic corruption linked to government contracts’’ with a new electronic procurement system called Prozorro ⁽⁷⁾. Recently, a similar step has been taken by buthanese procurement agency ⁽⁸⁾.

The financial institutions and FIDIC need to revise the MDB version 1999 and particularly Sub-Clause 15.6 related to fraudulent practices. FIDIC procurement guide also needs to be improved considering the 10 problematic points mentioned in Paragraph 3.

6 - Conclusion

Politicians definitely have a real challenge to reform their respective countries in order to stabilize the economy and reassure investors, construction companies and financial institutions.

There is a special need to improve roads infrastructure in numerous countries worldwide. Roads are a factor of economic development, tending to decrease poverty.

It is obvious that the financial institutions should improve their rules or provide guidance to the Clients having procurement issues. The success of roads projects will depend partially on the decisions made on procurement strategy.

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