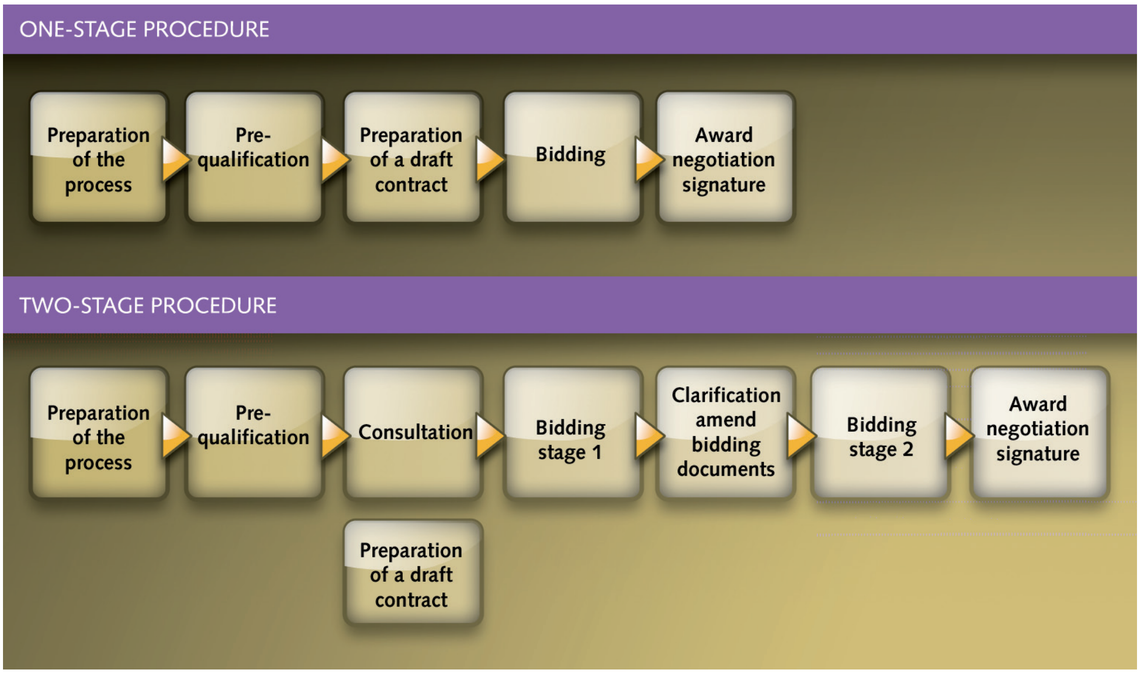
Concessions: Main steps in competitive bidding

Two main approaches can be chosen by the Government for the procurement of concessions:

- **One-stage procedure:** When the Government has a precise idea on the technical options and specifications to be chosen. Prequalified firms are asked to submit bids in strict accordance with the specifications imposed by the Government. Final selection is made on a "financial" basis alone and little room for negotiation is left to the selected candidate. This procedure is often used for highway projects.
- **Two-stage procedure:** In particular when uncertainties remain on technical options to be retained, it may be undesirable or impractical to prepare complete technical specifications in advance. This is typical for large and complex PPP projects. In such a case, a two-stage bidding procedure may be used. In stage 1, unpriced technical proposals based on a conceptual design or performance specifications are invited. They then are subject to technical and commercial clarifications and adjustments. In stage 2, amended bidding documents are issued and final technical proposals and priced bids are submitted and evaluated.

The main steps of each procedure are shown on the diagrams below. While preparation, prequalification and drafting of the concession contract are similar in both approaches, the main differences are found at the bidding stage.



Preparation of the selection process mainly consists in setting up the **Steering Committee and clarifying the approval process.**

Prequalification

Pre-qualifying bidders serves various purposes:

- On the part of the government, it ensures that only those capable of implementing the project to be put out to tender actually participate in the bid.
- On the part of the potential bidders, it saves an unqualified firm the substantial investment required to prepare a bid.

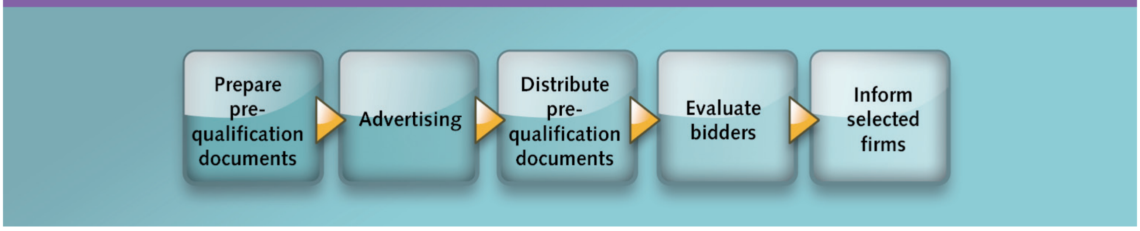
For experienced firms, it limits the number of competitors and eliminates inexperienced and unqualified bidders, thus reducing the risk of losing the project through an unrealistic bid (low balling). It therefore increases the incentive to participate.

In practice, however, and particularly in developing countries, there are two main issues;

- Prequalification can lead to collusion between potential bidders (moreover opinion within the World Bank seems to be moving against preselection);
- the problem is often not that there are too many bidders but that there may be too few candidates for the PPP project. Marketing the project is therefore of paramount importance to ensure that all qualified firms are aware of the project and feel confident they could benefit from it.

The steps involved in the prequalification process for a PPP are usually no different from those for typical civil works projects. Usually, 5 to 6 candidates are pre-qualified.

PREQUALIFICATION PROCESS



Two aspects are important for the pre-qualification process:

- the information provided to interested private parties,
- the information to be provided by the potential bidders:

Information to be provided by the public entity

This shall be sufficient to attract qualified private parties, allow them to assess their capability to satisfy the demands of the project and to allocate resources for bid preparation:

- short description of the highway project and main design features,
- scope of responsibilities to be entrusted to the private party,
- level of autonomy left to the private party,
- outline of the cost recovery mechanisms,
- project schedule and actual progress,
- principles of the selection criteria and process.

Information to be provided by potential bidders

In order to facilitate selection of the best candidates, they shall provide information on their:

- financial capacity and ability to raise private finance,
- managerial and technical capacity and expertise,
- certified experience of exercising similar responsibilities in similar projects,
- knowledge of the context of the project country,
- approach to the project and its specific conditions.

Typical pre-qualification documents

The pre-qualification documents should comprise:

Information on the selection process

Criteria to be used by the Steering committee to pre-qualify firms shall be clearly stated.

Project Information

- Brief description of the project and its main design features.
- Scope of responsibility to be entrusted to the private sector.
- Project schedules showing actual progress and next steps.
- Description of the institutional framework and the role of the various government agencies directly or indirectly involved.

Information to be provided by potential bidders

It is of vital importance for the project not to discourage applicants by unnecessary or unclear requests for administrative documents not directly related to the selection process. Request for document certification (legalizations, sworn and certified translations, etc.) should be kept to the minimum.

Financial sustainability of the applicant.

Typically, it must document its financing capability by submitting the following:

- A report on its financial situation (capital and net fixed assets)
- A report on the proposed financing structure for the project. Such a document, which should not be compulsory, could be used as a tool to analyze the applicant's understanding of the complexity of the project.

Experience and track record

Typically, a prospective bidder must provide the following evidence:

- that, either alone or as a member of a joint venture (J.V), it has undertaken one or more PPP projects of similar magnitude (to be defined in numbers).

- that its key personnel and that of its contractors have sufficient operational experience in the relevant activities of the project.

An important part of the relevant experience sought is for operation and maintenance, including general experience in the handling of public utilities. This is particularly important because of the impact of road operation on thousands of users.

Operating a public utility is very different from operating a typical industrial facility. It requires sensitivity to public perception and the development of a good relationship with the general public.

With regard to toll road operation and maintenance, relatively few companies in the world have enough practical experience thereof. In many developing countries, this expertise may need to be sought from foreign partners unless specific programs are conducted to develop domestic contractors (Module 3 -> PPP Policy Framework -> Capacity Building and Training-> Enhance Private Sector Capacity).

Management structures and operational capabilities

The prospective bidder typically provides information about its key personnel, particularly for project-managing the construction and handling the project's operation and maintenance.

Legal requirements

Bidders shall give evidence that they are not insolvent or in receivership and shall state that they have not committed any criminal offence relating to professional conduct. Information may be requested from the applicants about any pending legal claims against them and disputes they are involved in on other similar projects.

Due to the complexity and size of toll road projects, bidders are usually composed of several firms which will legally bind themselves together through some form of joint venture agreement.

Preparation of a draft contract

As the Concession Contract is the main document that will regulate the future relationship between the Government and the main private entity, it is preferable to embark on its preparation at an early stage in the process.

It should be noted that most countries around the world have developed model draft PPP contracts for each specialist sector or sub-sector. This means that the private sector has already had some input to draft contracts through consultation. It also means that both government and private sector will know what to provide and expect respectively as a basis for the specific project under consideration.

The active participation of legal experts from the country concerned is essential in drawing up draft (and final contracts). Additional and supporting assistance from foreign legal advisers is often required and advisable when the scope of the project goes beyond the traditional projects implemented in the country.

The advantages of including a draft contract in the bidding documents are numerous and include in particular:

- **Transparency and fairness.** Negotiation with the selected bidder on all terms of the contract would result in substantial changes in the conditions of contract between the firm and the contracting authority. Such an arrangement would be contrary to the principle of objectivity and equality and would surely be challenged by unlucky competitors.
- **Negotiation leverage:** Prior to a bid and during the submission period, bidders are under pressure from the other competitors. Moreover, they want the selection process to end as fast as possible to avoid unnecessary spending on project preparation: both reasons make them more likely to accept contractual clauses which they do not consider as being ideal. After the bid, it is normally the government which is in a hurry to get the project started. The winning bidder often wishes to delay contract finalization because it needs time to put together a management team and secure financing.
- **Risk assessment:** it allows the bidders to identify the risks allocated to them and further evaluate their potential impacts on expected benefits. On this basis, the private sponsors of the project will be able to discuss with other future actors of the project and negotiate the internal risk allocation with them.

Preparing the draft contract consists in translating the proposed risk allocation matrix into contractual terms that, once the agreement has been formally finalized, will govern project implementation. This exercise can therefore only take place when preliminary studies have been completed, the risk allocation and mitigation principles defined and Government support determined.

Bidding

Once a few competent firms have been selected and informed, the Steering Committee shall proceed with the bidding phase.

In the **Data room** all documents relevant to the project which will assist the firms in the preparation of their bids shall be made available in a common location managed by the steering committee.

All existing and reliable technical information on the project should be gathered in the data room. Objective project information on parameters largely influencing the project costs and revenue is particularly useful: traffic counts, Origin/Destination matrices, geotechnical investigations. All available study materials should be made available to the bidders and in particular:

- Economic and financial (pre-)feasibility study conducted on the project (Module 5 -> Due Diligence and Feasibility Studies),
- Detailed or preliminary design of the road (Module 2 -> Scope),
- Performance indicators for operation and maintenance (Module 2 -> Scope -> Performance Indicators for Maintenance Works),
- International and National standards governing the works, operation and maintenance. Description of the site location and access to the site (Module 3 ->

Sector Planning and Strategy -> Planning Process ->Technical and Performance Standards),

- Environmental impact assessment study (if any) and a detailed description of the constraints to be imposed on the private firms during all project phases (Module 3 -> Economic Development and Public Interest -> Mitigating Negative Impacts).
- Bidding documents will be compiled and sent out to the qualified bidders. A sufficiently long period (typically four months) will be allowed to the various bidders to collect information on the project and prepare their bids.

Technical information in the data room

Reference should be made in the bidding documents to the data room. Typically, bidders shall be informed on the location where the information is available, conditions to access it. A list of the main documents is also useful.

Financial and economic information on the project

- Statement of the financial requirements
- Proposed tariff, toll or fee structure and revenue-sharing arrangements, if any,
- Formulae and price indices to be used in the collection and adjustment of tariffs, tolls or fees,
- The currency in which bids may be expressed,
- Inflation, discounting rates, and foreign exchange rates for conversion of currencies to a common base for comparison,
- Information about rules and regulations governing foreign exchange remittance,
- Nature, amount, period of validity and other principal terms and conditions of security and warranties.

Information on project planning

- Timetable for completion of the construction works
- Maximum period for project construction
- Maximum concession period (if relevant)
- Timetable for project operation

Support from the Government

Specifications of the assistance and facilities to be provided by the government authority (Module 3 -> PPP Policy Framework -> Incentives ans Guarantees).

Bidding documents

Unlike for the procurement of works, supplies or services, international standards for PPP bidding documents have been slow to develop until recently. Some countries with long experience of PPPs such as the UK or Chile have compiled standard bidding documents for BOT or Concessions but do not necessarily apply them to all projects. South Africa, India, Pakistan, Zambia are among a number of countries that have more recently developed 'standardized provisions'. The main underlying reason is, once again, the differences that make each project unique and privilege customization over standardization.

The bidding documents sent to the pre-qualified bidders will include instructions to bidders. Along with other data, the instructions will outline, the required content of the bid, the procedures for clarifying the bidding documents and submitting bids, security requirements, how the bids will be submitted, opened and evaluated and the procedure to be applied for contract award and negotiation. A standard tender form is also supplied.

It is normally unnecessary to request a long list of tedious bid documents. Governments must beware of loading bidders with unnecessary requirements. Each item of the bid documents should have a clear, specific purpose. A simple way to view the bid submission is as follows:

- All bidders are pre-qualified and are therefore all capable of implementing the project.
- There must be some form of assurance that a bidder is truly committed to the project (bid bond and/or minimum committed equity).
- Information to be included in the bidding documents shall comprise:

Detailed instructions to the bidders to lead them through the bidding documents. In particular, instructions for bid submission (date, location) identify the project manager in the Government entity and relate to the relevant procurement legislation in force, if any. The procedure for contract award and negotiation, including evaluation methodology and criteria, is also detailed.

The evaluation criteria shall detail the method for the evaluation and comparison of bids, including how such factors may be quantified or otherwise evaluated and the method for evaluating alternative proposals.

Bid documentation

The bid documentation shall include three sets of document:

- Detailed requirements of the public entity,
- Complete information on the project and its environment,
- Instructions to bidders to prepare their proposal.

Detailed requirements of the public entity

This will be in line with the pre-qualification information and generally be in the form of a draft contract agreement, describing every public requirement:

Extensive definition of the responsibilities of the private party as regards highway design, rehabilitation, finance and maintenance,

- Level of autonomy of the private party,
- Risk allocation to the private party,
- Cost recovery mechanisms and conditions,

- Financial support to the project provided by the public entity.

Complete information on the project and its environment

- Description of the highway section,
- Specifications to be applied,
- Information relating to traffic conditions,
- Existing road condition surveys and results of recent investigations (pavement, structures, drainage, road furniture, landscape) relating to the project,
- Legal and administrative framework.

This information shall be detailed in order to minimize bidding costs for the private candidates but shall not:

- prevent bidders from offering cost-efficient alternatives based on their expertise and capacity for innovation,
- transfer unnecessary risks to the public entity.

Instructions to bidders to prepare their proposal

These instructions will specify:

- What documents bidders must produce regarding their technical and financial proposals,
- What information they shall give concerning their own organization for the project and its set of internal agreements,
- What guarantees they shall present with their bids,
- What mechanism will apply for exchanging information between the public party and the candidates during the bidding period,
- How long the tender period and the selection procedure will last,
- Which criteria will be used to assess their proposals.

The public entity should make sure that its tender specifications will enable private candidates to make comparable proposals which will satisfy the main objectives of the project.

Documents to be submitted by bidders

Technical proposal

- Operating program and costs
- Maintenance program and costs
- Environmental protection plan.

The identification of contractors, sub-contractors and suppliers with their qualifications is an additional and unnecessary burden on bidders and should not be compulsory. The construction market is sufficiently well developed and competitive for those actors to be identified once the concession has been awarded.

Similarly, bidders should not be requested to conduct a detailed engineering design of the project.

Financial proposal

- Cash flow projections: although usually not directly used in the evaluation, such projections can show whether the bidder has used reasonable assumptions in the preparation of his bid. They can also provide an indication on the level of detail of the investigations conducted by the bidder.
- Formal bid - proposed tariff, payment to government or requested amount of subsidy.

Legal proposal

- Acceptance of terms of the contract,
- Draft shareholders' agreement, consortium agreement, joint venture agreement or a similar contract by which the sponsors commit themselves to carrying out the project agreement if they are awarded the project, could be requested,
- Letter of conveyance signed by the authorized representatives of the company or consortium submitting the bid.
- Term sheets of other main contracts could also be requested (construction contract, operation & maintenance contract, insurance, etc.).

Draft Contract

Bidders may also be required to submit a copy of the draft contract, as part of their bid documents, in order to affirm their compliance with the terms of the contract and limit post selection negotiation to a reasonable minimum. Such a provision is usually made when the Government wants to limit future negotiations on the terms of the contract to the minimum.

Bid evaluation

Months and possibly even years of work reach their climax during bid evaluation. For the losing bidders, months of work and considerable investment may be considered as "wasted". If they suspect they have not been treated fairly by the government, many bidders will not hesitate to challenge the bid evaluation process. There have been suggestions to mitigate this risk, including compensating the losers to cover part of their expenses. Such provisions are successfully implemented for PPPs in some countries such as Holland and in other types of competitive bidding such as international architecture competitions. However, it is regarded as complex to do this and has not been tried elsewhere.

Evaluation criteria

Evaluation criteria will cover (i) compliance of the bids to the tender specifications, (ii) feasibility of the proposals, (iii) costs and benefits of the proposals for the public entity.

Bid Compliance

Strict verification of compliance is necessary if the public entity wishes the contract award process to be transparent. Compliance shall apply for both technical and financial proposals. Alternatives shall also be analyzed on the grounds of compliance and should not depart from the compulsory specifications.

Proposal Feasibility

Technical feasibility will be evaluated against prescribed performances on the basis of standards, methods, duration of construction, associated risks, certified design, rehabilitation and maintenance experience, proven ability in environmental impact mitigation, traffic management, health and safety arrangements. Cost analysis and comparisons will be key elements in this examination.

Financial feasibility will be analyzed through a detailed review of the basic assumptions of the bids (realism of the project revenue -if any- as compared to all costs involved, credibility of financial support, existing guarantees and commitments within the groups bidding).

Value for Money of Proposals

Making a transparent evaluation of the "value for money" of each proposal for the public entity and comparing them on equal terms is a difficult process:

- the first element is the financial support (explicit or implicit) given by the public entity to the project, either immediate or deferred.
- all other elements of costs and benefits, such as tolls levied, time savings, VOC savings, increased comfort and safety for users, tax revenue for the State have to be calculated at net present value, using common assumptions.

Selection of Preferred Bidder

This shall be based on a combination of the quantitative assessment of the "value for money" and an evaluation of the risks of non-feasibility of the proposed solutions. The difficulty of assessing bids for complex projects should in no case lead the public entity to rely on over-simplified integrated quotations.

Bid evaluation: Using the criteria and the methodology stated in the bidding documents, the steering committee will select the best proposal.

Evaluation rules

Objectivity in the comparison of bids should be a leading principle when drawing up the evaluation rules. The first step (validation) of the evaluation consists of checking compliance of the bids with the technical, financial and legal specifications of the bidding documents. This step is conducted on a pass / fail basis. Evaluators should focus on the feasibility of the project rather than on the bidding firms who are supposed to have demonstrated their capacity to implement the project in the pre-qualification stage. It should be noted, however, that while validation helps reduce the risk of project failure, it may also have important drawbacks. It often involves considerable discretion and judgment by the evaluation committee, which reduces the overall transparency of the project.

The second step (financial evaluation) of the evaluation will compare the compliant bids among each others, using objective and quantifiable evaluation criteria.

Financial evaluation criteria

The choice of an appropriate financial criterion greatly depends on the project. It should have been identified at an early stage of the evaluation process and clearly stated in the bidding documents.

Typical bid evaluation criteria are:

- Toll rate for the first year of operation (usually, a toll rate escalation formula is also provided),
- State subsidy required,
- Duration of the concession,
- Income guarantee requested from the State,
- Revenue offered to the State for existing infrastructure facilities,
- Total income from the concession,
- Degree of risk commitment that the bidder assumes during the construction stage,
- Quality of the technical offer

Multiple-parameter bids

In some cases, bids are evaluated on the basis of multiple parameters; each bid is scored using a formula that aggregates the various parameters with chosen weighting coefficients. Such a system has the advantage of better taking into account the complexity of PPPs and balancing out the advantages and drawbacks of each proposal.

The reference provided below contains a table showing the various parameters and the corresponding criteria used for the procurement of toll roads in some European countries.

Analysis of Highway Concessions in Europe, Franck Bousquet, 1999, section III.4

The problem with this procedure is its inherent subjectivity. Typically, questions may be raised on the relative importance given to a particular parameter as opposed to another. Complexity of the evaluation system does not necessarily lead to more objectivity. Moreover, regardless of the complexity of the evaluation formula, bidders will always have the resources to mathematically analyze the formula and use its weaknesses to prepare a bid that would optimize their chances, not necessarily in the interests of the project.

Single parameter bids

Experience has shown that selection systems based on a single parameter are often the most successful.

The criterion is usually chosen from among the following:

- A bid based on the initial toll rate. The lowest wins.
- A bid based on a payment to (or a subsidy from) the government. In this case, the initial toll rate is set by government. The highest payment (or lowest subsidy) wins.
- A bid based on the length of the network to be built. Again, the initial toll rate is set. The bidder which proposes to build the longest network wins.
- A bid based on the term of the concession. The initial toll rate is set. The shortest concession term wins.

The table below shows the evaluation criteria chosen to award various road concession projects in Latin America.

AWARD CRITERIA IN SELECTED LATIN AMERICAN TOLL ROAD CONCESSIONS

Country	Award criteria	Concession duration
Argentina-road corridors	Highest lease fee paid to government	Fixed by government but extended after renegotiation
Argentina-urban access	Lowest toll	Fixed by government but extended after renegotiation
Brazil-Federal	Lowest toll	Fixed by government
Brazil-Sao Paulo	Highest lease fee paid to government	Fixed by government
Brazil-Parana	Largest network length	Fixed (but likely to be extended as a result of politically imposed cut in toll)
Chile-1st generation	Multiple criteria	Fixed by government
Chile-2nd generation	Least net present value	Unknown
Colombia-1st generation	Multiple criteria	Fixed by government
Colombia-2nd generation	Least cost to government	Fixed by government
Mexico	Least cost to government	Fixed by bid
Peru	Shortest term	Fixed by bid
Peru	Least subsidy	Fixed by government
Uruguay	Shortest term	Fixed by bid

Sources: Estache (2000), Irigoyen (1999) and various World Bank internal reports.

Evaluation based on the initial toll rate has the distinct political advantage of securing a bid with the lowest possible toll rate. Particularly in countries where there is substantial resistance to the payment of tolls, this procedure is the most socially acceptable. Moreover, by giving an incentive to lower the toll rates, such a process is likely to bring more vehicles on the road and maximize its economic benefits.

The other side of the coin is that reduced toll rates penalize the revenue stream of the project, in particular in its early years when financial equilibrium is particularly difficult to achieve. Under pressure from competition, bidders can be too aggressive in their bids and if selected, might find themselves in a position where they are not able to secure the required sources of funds (debt in particular). Such circumstances would result in substantial delays for the project.

Systems based on a fixed initial toll rate and bids evaluated on the basis of the highest payment made to the Government (or lowest subsidy required) sometimes appear more reasonable. They have the advantage that the government controls the initial toll rate and sets it at a level which is both acceptable to road users and will still generate sufficient revenues to mobilize the required financing. It is however very difficult for the policy makers to set the toll rate at an optimum level whereby financial balance of the operating company is relatively secured and only the profit of shareholders is at risk.

Experience of the Chilean Government in the bidding process is commented in:

Broad Roads in a Thin Country: Infrastructure Concessions in Chile. A. Gómez-Lobo and S. Hinojosa. Draft paper. 1999

Route 68 Concession, Chile (PVR auction), World Bank

Comparison of single evaluation criteria used for eight different projects:

Private Financing of Toll Roads, Fishbein and Babbar, RMC discussion papers series 117, page 21.

Contract Negotiation and Award (one-stage procedure)

The bid evaluation process shall be concluded by the elaboration of a bid evaluation report summarizing the outcome of the evaluation and the identification of the bidder to be called to negotiate.

Once again, the complexity of PPP arrangements makes this phase very delicate for the following reasons:

- Issues to be discussed are very numerous, diverse and interrelated. PPP negotiations always last several months.
- Detailed expertise on all fields relating to the project is required on both sides of the negotiating table. On the Government side, financial, legal and technical experts shall closely follow the entire process to gain a good understanding of the overall picture.
- Investment from Government at this stage has already been substantial.
- Steering Committee members are usually under pressure from Government to quickly conclude and start the implementation phase.

- Numerous unclear areas have to be clarified.

In concessions where substantial investment is required from the firm, the most sensitive issue lies with the capacity of the bidder to secure the financing of the project. While the project equity is usually to be mobilized by the bidder from its own resources, debt provided by the lenders (typically 60 to 80% of the project cost) is not firmly committed at this stage. In reality, there is no guarantee that financial closure (final commitment from financiers on the total project cost) will be reached. Requesting firms to include these commitments in their bids (full underwritten bids) is unrealistic since this would cost around ten times more to the bidders than for a normal bid and most firms would not be willing to take such risk.

Typically, the concession contract is signed upon agreement by both parties on all clauses and its enforcement is subject to financial closure being obtained by the concessionaire within a fixed period of time.

There is no guarantee however that such a financial closure will be reached and the contract shall become void if the concessionaire cannot mobilize sufficient funding.

For larger and technically difficult projects, the two stage procedure is to be recommended.

Contract Negotiation and Award (two-stage procedure)

This procedure is made to allow the private sector to come up with technical alternatives and options that would improve the project design before conducting the actual selection.

In a first stage, bidders are requested to submit technical bids only, based on a conceptual design made by the Government. A draft contract is usually also included in the bidding documents and possibility is given to the bidders to comment and amend it. No selection is made at this stage, its main purpose is to gather information from bidders and improve the project design. The steering committee can then conduct a series of individual discussions with the bidders and request them to clarify, justify or document their proposals.

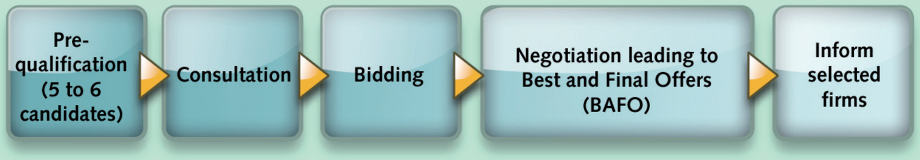
In a second stage, the Government finalizes the project design on the basis of the best proposals identified with the bidders and prepares new bidding documents and invites the participants to submits full technical proposals and priced bids as in the one-stage procedure.

The main drawback of such procedure is the lack of motivation sometimes noticed from the bidders to prepare sound and comprehensive technical bids in the first stage while no selection is made, and disclose information on their approach to the project to other bidders who could use it in the second stage.

The negotiation procedure

The procedure detailed below has been developed by various public organizations to improve the outcome of the negotiation phase and reduce the risk of unsuccessful tenders. Even though this selection procedure has largely been developed so as to fit in with European Union legal requirements, the principles are easily adaptable to other jurisdictions.

THE NEGOTIATION PROCEDURE



As in the two stages procedures, all pre-qualified bidders are requested to submit a technical bid based on a conceptual design. However, the technical proposal comes with a priced bid. Two candidates are selected from the bid evaluation process (pass/fail for the technical proposal and lowest bid for the price). The option of starting negotiations with three parties should be avoided as this would complicate the procedure unnecessarily for all parties.

The negotiations should result in the client asking the two short-listed bidders to submit new offers (Best-and-Final Offer - BAFO) on the basis of the risk allocation and technical terms that have been developed with the two candidates in parallel.

Again ultimate selection criteria should be price and the strength of the financial package.

The final negotiation phase with the preferred bidder (the other candidate should remain in reserve) should finalize actions, certain due diligence aspects by the preferred bidder in order to settle the final risk sharing and give the preferred bidder time to arrange financial close or possible acquisition.