SWISS CHALLENGE PROCUREMENT

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Building a better working world

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Swiss Challenge Procurement: *Background*

- Worldwide, private sector participation in developing infrastructure with the government through PPP/PFI, has increased
- Generally infra projects are conceptualized and planned by government and private sector comes in during project financing and implementation
- Sometimes private sector itself conceptualizes & plans the project and submits unsolicited proposals for development of infrastructure projects to governments to get the required official approvals
- Government faces challenge in evaluating such unsolicited projects due to lack of competition and transparency
- The most common system that governments use to manage unsolicited proposals is Swiss challenge.

Governments are under no obligation to accept unsolicited proposals, but economic and political conditions compel them to consider it.

Swiss Challenge Procurement: *Definition*

"Swiss Challenge Procurement" means

- a Private Sector Participant (Original Project Proponent) submits an Unsolicited or Suo- Moto proposal…
- …the proposal is accompanied by draft contract principles for undertaking a Project…
- …the project is not initiated by the Government Agency or the Local Authority and…
- …the Government Agency or the Local Authority then invites competitive counter proposals in such manner as may be prescribed by the Government.

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Swiss Challenge Procurement: *Process*

Submission of Unsolicited Proposal → Approval of Preliminary Proposal → Negotiation → Bidding, Counter-proposal & Award

Unsolicited Proposal

Submission of Unsolicited Proposal | Approval of Preliminary Proposal | Negotiation | Bidding, Counter-proposal & Award

Constituents of Unsolicited Proposals

- Feasibility study including market analysis, technical aspects, financial analysis, economic analysis and operational/institutional aspects;
- Basic contractual terms and conditions;
- Pre-qualification requirements, including legal requirements, experience or track record and financial capability to undertake the project;
- Preliminary financing plan, which describes how the project will be financed; and
- Implementation plan, which would show the timeframe of construction and implementation.

Preliminary Evaluation

Submission of Unsolicited Proposal	**Approval of Preliminary Proposal**	Negotiation	Bidding, Counter-proposal & Award

- Governments typically use a short initial period to screen out unnecessary proposals;

- Process allows proponents to test concept without putting large resources into the project development;

Negotiating terms of unsolicited proposal

Submission of Unsolicited Proposal → Approval of Preliminary Proposal → **Negotiation** → Bidding, Counter-proposal & Award

Open Tender	In case the original proponent and the Government do not mutually agree on the terms and bid for the project, the Government has the option to invite bids from the open market
Direct Negotiations	Government, can negotiate with the original proponent regarding the project idea.
IPR*	Government has the option to buyback the intellectual property rights (IPR) to key approaches or technologies, proposed by the original proponent.

Bidding process

Submission of Unsolicited Proposal → Approval of Preliminary Proposal → Negotiation → **Bidding, Counter-proposal & Award**

- Detailed Project Report is prepared by the organization ("Originator") at its own cost (which is likely to be reimbursed by the government/ lowest bidder) ;
- Technical scheme and specification developed by the Originator;
- Government body/ agency puts above in public domain and invites on a global basis proposal/ quotes on above;
- The Originator needs to match most competitive/ least quote and get the project (last right of refusal). If matched, the project is awarded to Originator;
- If the Originator does not match the most competitive/ least quote the project awarded to the most competitive bidder

Cost of Bid Process Management

Submission of Unsolicited Proposal → Approval of Preliminary Proposal → Negotiation → **Bidding, Counter-proposal & Award**

- In case the original proponent manages to win the project, the government will fully reimburse the cost incurred by him for compilation of Project idea and various studies conducted;

- If the original proponent is not the lowest bidder, then the cost will be reimbursed to the original proponent by the lowest bidder.

Pros and Cons of Swiss Challenge Procurement

Pros

- Very useful where governments have limited technical and financial capacity to develop projects
- Promotes innovation and incentivizes to propose new ideas
- Reduces transaction cost
- Faster implementation in case of project award to originator
- Incentivizes private sector participation
- Potential route for furthering local projects that are not national priorities

Cons

- Risks related to sufficient transparency or competition
- Legal validity of using the Swiss challenge when a counterproposal contains different specifications than the original proposal
- Bidding asymmetry due to time given to bidders to prepare counter proposals vis-à-vis time taken by originator for preparation
- Difficult to measure value for money for unsolicited proposal due to want of comparable competing bid
- No assurance that unsolicited bidder won't withdraw its offer

Swiss Challenge Vs. Formal Competitive Bidding

Parameter	Swiss Challenge	Competitive Bidding
Conceiving project idea and project planning	Private Sector	Government
Negotiation of terms with private sector before tendering	Yes	No
Bid process management	Government	Government
Cost of bid process management	Borne by government if original proponent wins the bid; else winner of the bid	Borne by government
Right to match the bids	Original proponent has the right	No such right

Challenges which continue even in Swiss Challenge

- Adequate socio-economic cost benefit analysis before selection of project
- Proper disclosure of all information, to the applicants, in the bid document
- Lack of coordination among agency/ ministries
- Delay in land acquisition, environmental clearances, etc.

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Applicability of Swiss Challenge on Indian infrastructure

National Level Policies

- Draft PPP Rules, 2011 issued by Department of Economic Affairs, Ministry of Finance
- National Public Private Partnership Policy issued by Department of Economic Affairs, Ministry of Finance

State Level Initiatives

- Different states have taken initiatives to formulate regulations for treating unsolicited proposals / Swiss challenge
  - Gujarat
  - Rajasthan
  - Punjab
  - Andhra Pradesh
  - Madhya Pradesh

Draft PPP Rules, 2011

Unsolicited proposals may be accepted only in exceptional circumstances and only if the project satisfy the following conditions:

- Project should not:
  - require any form of guarantees from any national or state or local government or its agencies,
  - require transfer of ownership of land of the Central or State or local government or its agencies, and
  - have been identified earlier by the Contracting Authority, as duly documented in its published plans or in any of its official document.
- Project should:
  - involve use of proprietary technology, or new or innovative technology or design, or it provides a new and cost-effective method of service delivery.
- Project involves delivery of facilities or services to:
  - predominantly (at least 50% of coverage) rural or peri-urban areas or population below poverty line; or
  - public healthcare or education or public shelter or vocational training or rural information technology.

Source: Draft PPP Rules, 2011

National Public Private Partnership Policy

- Unsolicited bids/Swiss Challenge proposals are not preferred by the Government.
- The discomfort with the use of unsolicited proposals in the public sector is on grounds of lack of transparency, and lack of fair and equal treatment of potential bidders.
- There are elements of "*informational asymmetry*" and "*bidding asymmetry*" between an Original Proponent (OP) and its competitors.
- The bidding asymmetry is due to time and price asymmetries. Since only the OP essentially gets an opportunity to make the BAFO (Best and Final Offer) after one or more rounds of negotiation–an opportunity that is denied to its competitors who are not authorized to submit an equal number of negotiated responses.

In exceptional circumstances, in sectors not traditionally associated with PPP structures or where procurement of proprietary technology is involved, variants of the approach could be considered for development, with prior approval of the competent authority, provided the VfM analysis establishes such a decision.

Source: Draft PPP Policy, 2011

Swiss challenge framework in different states Rajasthan

- Rajasthan Public Private Partnership Guidelines, 2012 are silent about Swiss Challenge

- Rajasthan's Public-Private Partnership Policy-2008 and Social Sector Viability Gap Funding Scheme of 2007 permit the government to approve the scale and scope of a suo- motu proposal or project undertaken through "Swiss Challenge" approach, but both these policies are silent on the modalities of implementation and selection of private partners through the "Swiss Challenge" route.

- The Rajasthan Road Development Act (RRDA) offers better guidance for receipt and processing of unsolicited proposals in that it allows for the receipt of such proposals where no scheme has been initiated for the development of any road

Source: Rajasthan PPP Guidelines; Rajasthan's Public-Private Partnership Policy-2008; Social Sector Viability Gap Funding Scheme of 2007 ; Rajasthan Road Development Act (RRDA)

Swiss challenge framework in different states Andhra Pradesh

- The Andhra Pradesh Infrastructure Development Enabling Act (the APIDE Act) allows for adoption of the "Swiss Challenge" approach in cases of projects being where

  - the Government or government Agency will be required to provide asset support
  - financial incentives in the form of contingent liabilities or direct financial support are required to be provided
  - exclusive rights are conferred on the Developer
  - extensive linkages i.e. support facilities for the project such as water connection etc. are needed

Source: Andhra Pradesh Infrastructure Development Enabling Act

Swiss challenge framework in different states Gujarat

- Gujarat is the first state in India to introduce a de-facto "Swiss Challenge"-based procurement procedure for the award of directly negotiated proposals

- Under section-10 of GID Act unsolicited proposals which does not require state subsidy are processed through this route. It involves three stages:
  - Acceptance of the project by the Government and that it can be delivered by the developer in a time frame
  - Detailed negotiations to arrive at a consensus on the project parameters including the price. competitive bidding on functional specifications of the project taken as fait accompli
  - If better proposal (s) is received, the original proponent is given the opportunity to make his proposal competitive with that. If he fails, the project goes to the selected bidder. The project development costs can be reimbursed

Source: GIDB website, GID Act

Swiss challenge framework in different states Punjab

- Under Section 37 of Act Punjab Infrastructure (Development and Regulation) Act, any potential contractor can submit an unsolicited proposal, according to its own choice, to the Punjab Infrastructure Development Board (PIDB) for taking up work on any infrastructure project.

- This act enables PIDB to accept any such proposal on a provisional basis, submitted by an individual or agency which would involve a new concept or technology.

- After entering into a provisional agreement, a public hearing would be conducted by the quasi-judicial body – Punjab Infrastructure Regulatory Authority (PIRA) – to be constituted in the next few days.

- The agency would play a regulatory role to safeguard the interests of construction companies. If other party comes forward to work on better conditions, the initial bidder would be allowed to amend his proposal within 30 days and the contract would be signed with him to execute the work. If he failed, the concession agreement would be signed with the second bidder.

Source: Punjab Infrastructure (Development and Regulation) Act

Swiss challenge framework in different states Madhya Pradesh

- Madhya Pradesh Infrastructure Development (Swiss Challenge) Guidelines were issued in 2014

- The guidelines require evaluation of the unsolicited proposal, relating to the eligible sectors (as defined in the guidelines), by the State Level Empowered Committee (SLEC) and relevant State Govt. department /a board /a local body/ a state Govt. controlled body concerned with the project

- The evaluation process for the unsolicited proposal shall be initiated by the authority only if:
  - there is no current project and development plan in process for the similar project.
  - there is certain need for the project.
  - the project proponent fulfils the qualification criteria.

Source: Madhya Pradesh Infrastructure Development (Swiss Challenge) Guidelines 2014

Swiss challenge framework in different states Madhya Pradesh

- Unsolicited proposals shall not be considered for evaluation if:
  - The need can be established with known and reasonable limits and the proposal could be done by traditional bid process management.
  - Financial Assistance from government by way of Viability Gap Funding (VGF) is more than 20% for project excluding the cost of land.
  - There is conflict with the enforced laws.

- The cost related to preparation of the DPR shall be reimbursed to the project proponent by the authority, only in case the authority decides not to proceed with the project after floating the tender.

- Guidelines endeavor to complete entire evaluation process within 8 months and award within 12 months

Source: Madhya Pradesh Infrastructure Development (Swiss Challenge) Guidelines 2014

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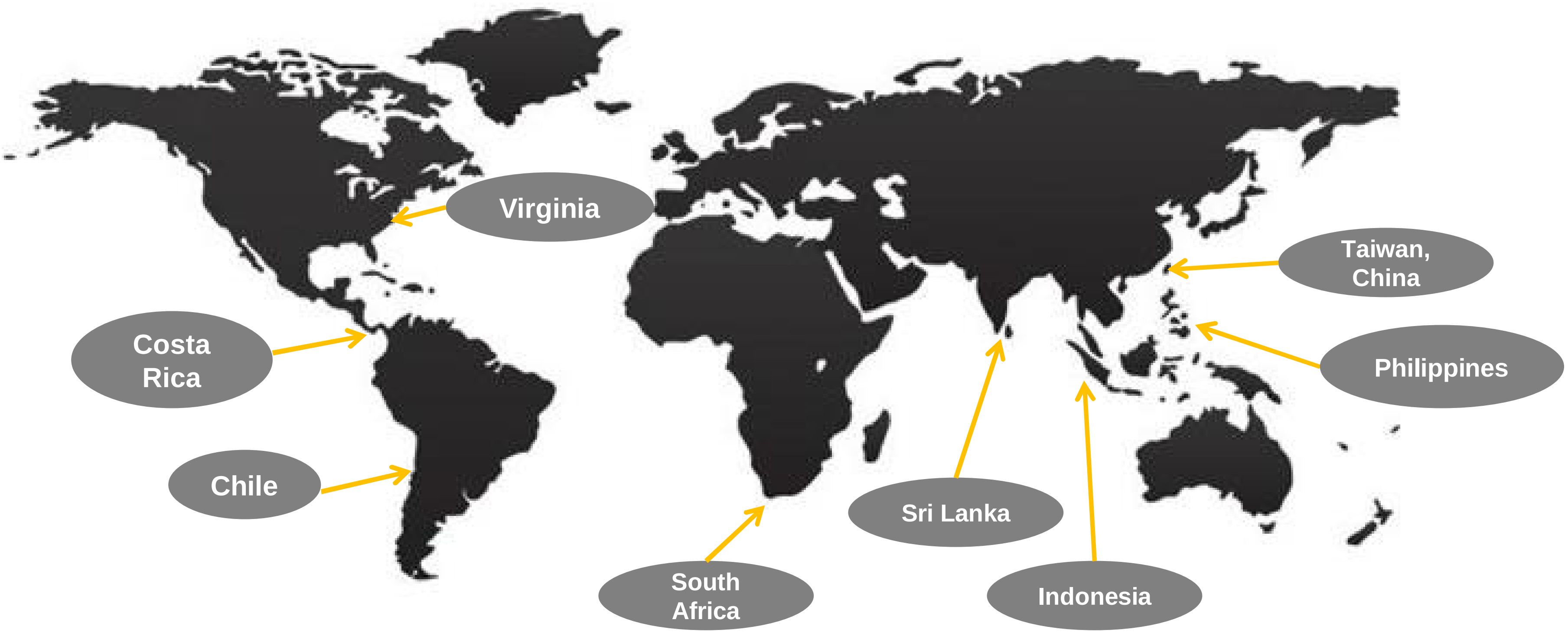
Few countries that have used Swiss Challenge Scheme in transportation infrastructure sector



A number of South-Asian countries are also using Swiss Challenge as a mode to develop infrastructure

Few examples of countries where Swiss challenge system has been used

Unsolicited proposal: Philippines

- Under the Philippines Build–Operate–Transfer (BOT) Law, national or local authorities were able to accept unsolicited proposals for BOT projects on a negotiated basis if:
  - The project involves a new concept or technology and is not already listed in the roster of priority projects identified by the government;
  - No direct government guarantee, subsidy, or equity is required;
  - The project is submitted to a *price test* or “Swiss challenge” from competitors;

- The price test works as follow:
  - the agency awarding the project must invite comparative proposals to any unsolicited proposal it has received;
  - the invitation to tender must be published in a newspaper of general circulation;

Source: PPIAF, World Bank

Unsolicited proposal: Philippines

- The published invitation must inform potential bidders where to obtain tender documents;
- Competitors have 60 days to submit competitive proposals;
- If a lower-priced proposal is received, the original proponent has 10 days to match it and win the contract. Otherwise, the award goes to the lowest bidder;

- Procedure:
  - On receipt of an unsolicited proposal, the agency must invite comparative bids.
  - The invitation must be published in the telegraph.
  - Within 60 days competitive bids are to be submitted and within 10 days of such receipt, the original proponent has to match or better the lowest bid.

Source: PPIAF, World Bank

Unsolicited proposals: Indonesia

- As per Chapter VI of Presidential Regulation Concerning Government Cooperation with Business Entities in the Supply of Infrastructure (No. 67 of 2005), business entities are allowed to propose projects that are not included in the list of priority projects

- The minister, institution head, or regional head evaluates the unsolicited proposal for:
  - suitability with the national or regional medium-term development plan and the infrastructure sector strategic plan;
  - suitability of the project location with the regional spatial plan
  - the relationship among infrastructure sectors and among regions, and
  - the cost analysis and social benefits.

Source: PPIAF, World Bank

Unsolicited proposals: Indonesia

- The Indonesian system rewards the original proponent in one of two forms:
  - By granting the proposal an added value (bonus) not to exceed 10 percent of the proponent's tender and to be openly announced before to the procurement process, or
  - By purchasing the project proposal (including intellectual property rights) by the government or the winner of the tender.

- In both cases, the minister, institution head, or regional head determines the amount of added value or the value of costs to be reimbursed to purchase the project proposal, based on the consideration of an independent appraiser before the procurement process.

Source: PPIAF, World Bank

Unsolicited proposals: Korea

- Private Participation in Infrastructure (PPI) passed in 1998 allowed the following incentives for the initial proponent:
  - bonus evaluation points,
  - minimum revenue guarantees, and
  - foreign exchange guarantees

- To reduce the number of unsolicited proposals[@] following procedures were introduced in Korea:
  - Mandatory consultation between PIMAC and the line agencies or ministries, were introduced at every stage of the implementation
  - feasibility of every project should be reviewed and screened through a VfM test
  - Provisions for minimum revenue guarantee[@@] were removed

[@]Between July 1999 and April 2006, PICKO/PIMAC received approximately 141 unsolicited proposals with project costs estimated at $40.4 billion;

[@@] Previously, minimum operating revenue guarantees (MRG) were 80 % of operating revenue for the first 5 years of operation, 70 % during the 6 to 10 years after commencement of operations, and 60 % from years 11 to 15. However, since 2005, these guarantees no longer apply. Source: PPIAF, World Bank

Case Study on Yongin-Seoul Expressway, Suwon City, South Korea

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Project Background

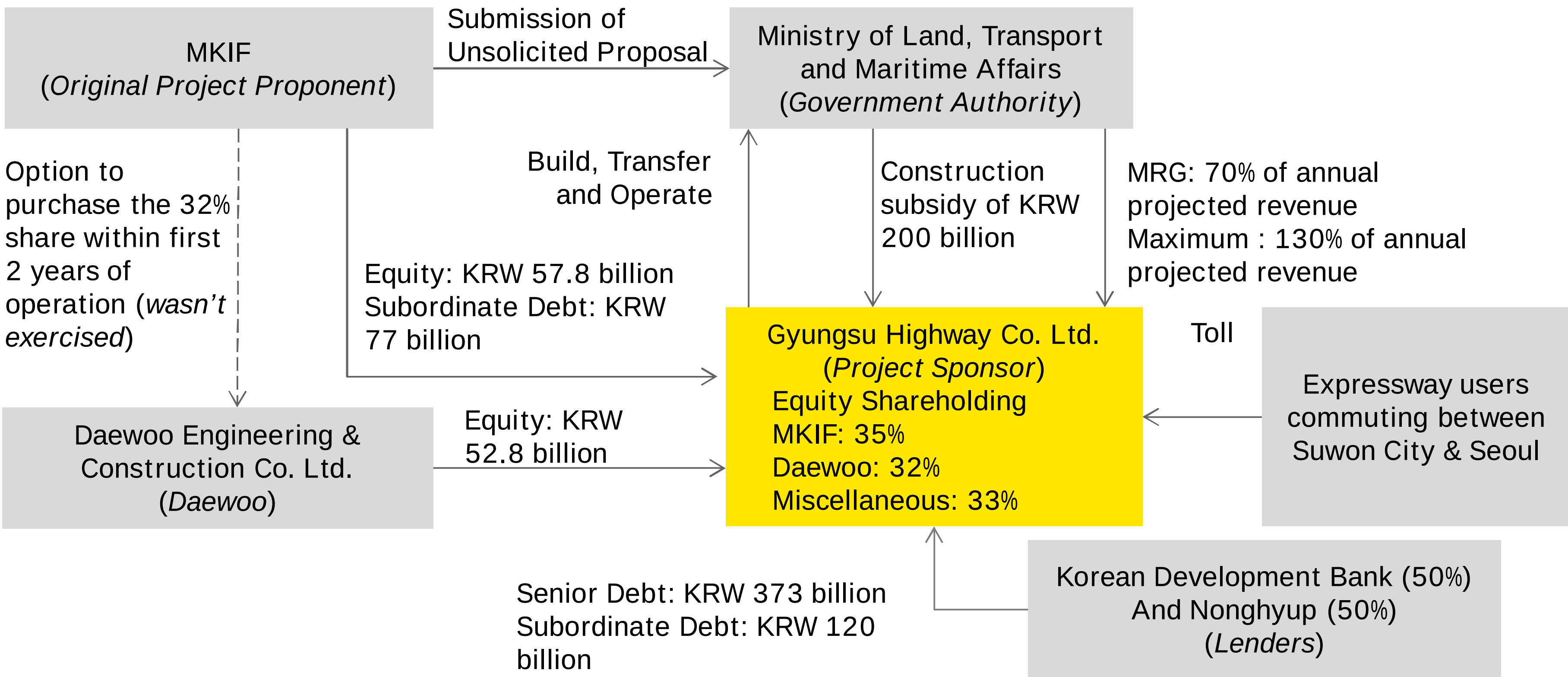
- Yongin-Seoul Expressway (YSE) was constructed with an aim to relieve traffic congestion along the Seoul-Busan Expressway which was struggling with the heaviest traffic in South Korea.
- 23 km tolled 4 to 6 lanes expressway connecting Suwon City to Seoul consisting 10 tunnels and 21 Bridges.
- An unsolicited proposal for the construction of the expressway was submitted by Macquarie Korean Infrastructure Fund (MKIF) in 2002 as a Build, Transfer and Operate (BTO) tolled highway to Ministry of Land, Transport and Maritime Affairs (MLTM), South Korea. The contract was awarded through a competitive bidding process in January 2005.
- The construction was completed with 44 months at the project cost for KRW 940 billion. The concession period is for 30 years including 10 year minimum revenue guarantee. The expressway was opened to public in 2009.
- The project is currently under operation with actual traffic volume close to 90% of the projected traffic volume (as per concession agreement).

Evaluation of Unsolicited Proposal as per PPP policy of South Korea

1. Submission of Project Proposal *(By OPP)*
2. VFM Test *(By PIMAC)*
   September 2002
3. Notification of Project Implementation *(By Competent Authority)*
   March 2003
4. Announcement of RFPs *(By Competent Authority)*
5. Submission of Project Proposals *(Potential Bidders)*
6. Evaluation and Selection of Preferred Bidder *(By Competent Authority)*
7. Submission of revised proposal *(By OPP)*
8. Negotiation and Contract Award *(By Competent Authority)*
   Jan 2005

Transaction Structure

- 4-6 lanes, 22.9 km included 10 Tunnels and 21 Bridges
- Project Cost: KRW 940 billion. Debt to Equity Ratio 60:40
- Construction Period : 44 months, Concession Period: 30 Years (*from opening*)
- Supported by Minimum Revenue Guarantee (MRG) for the first 10 year of operations
- Approximately 22-minute reduction in transit time, expected economic benefit KRW 88 billion/year
- Opened to Public in 2009



Key Learning

Proactive private sector participation to establish public needs

- The need for highway to decongest the Seoul-Busan Expressway was on Government's agenda for long; however only due to pro-activeness of the project developers did the alternate route became a reality.

Cost effective solution

- As per Korean Development Institute the project is saving approx. KRW 88 billion per year due to use of environmental friendly design and decongestion of existing highway.

Innovative Government Support

- The Korean Government in effort to encourage private sector participation enabled the Minimum Revenue Guarantee Scheme (which it has abolished now for future projects) and land acquisition process was conducted by MLTM.

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Lessons for India: Unsolicited proposals....

Legal Framework

- Develop a policy on Swiss challenge / unsolicited proposals from the private sector and align them with CAG, CVC & other regulations
- At the international level UNCITRAL provides a legislative system for unsolicited proposals.

Capacity Building

- There is need to educate and institutionalize capacities to evaluate proposals on Swiss challenge

Transparency in information sharing

- It is important that authority understands what information to be shared and what not to ensure transparency in bidding process

Time bound approvals

- Incentive for Swiss challenge can only work, if related approvals are time bound

Swiss challenge presents an effective way to incentivize private sector in project conceptualization & planning, what needs is adequate legal ? Regulatory framework

Thank You

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