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EIC
EUROPEAN INTERNATIONAL CONTRACTORS

EIC *Discussion* Paper on "Classic Infrastructure"

for the

Second EU-Africa Business Forum in Accra (Ghana)

Introduction

"European International Contractors" (EIC) is an industry association that represents the interests of the European construction industry in all questions related to its international construction activities. EIC has construction industry federations from 15 European countries as its members and the **international revenues** of European contractors affiliated to EIC Member Federations amounted in the year 2005 to some **100 billion €**.

It has been widely acknowledged that the **improvement of infrastructure connections in Africa**, i.e. the transportation networks as well as the promotion of private sector participation in the delivery of electricity, water and sanitation services, is a precondition for achieving the ***Millennium Development Goals*** in Africa. The European Commission estimates that between 2005 and 2015 Sub Sahara Africa needs to spend approximately 5% of its GDP on infrastructure investment and a further 4% on operations and maintenance – additional expenditure of **20 billion US$ per year**.

Reasons for European disengagement from Africa

Since 1990, European international contractors have doubled their international turnover from then 53 billion US$ to some 120 billion US$. However, the same statistics reveal that only 5% of overseas works is carried out nowadays within Africa - compared to 15% in 1990. The main reasons for the withdrawal of European companies from Africa are the following:

1. **A sharp reduction by African governments and development aid agencies of the share of resources allocated to infrastructure during the 1990s**. The European Commission has noted recently that also EU Member States' support for economic infrastructure and services has declined over the last decade, mainly in transport and partly in energy.

2. **A strategic realignment of the development policy of Multilateral and Bilateral Development Banks** which are shifting their financial support from project aid to **budget support** and the procurement rules from internationally harmonised Standard Bidding Documents to a rather diverse range of **Country Procurement Systems**.

3. **The growing importance of the financial markets as well as Corporate Governance requirements** motivated European infrastructure providers to focus on business profitability. This lead to a concentration of activities on those foreign markets with a business-friendly legal framework and minimum political and economic risk as well as an evolution of many European contractors into construction-related service providers.

4. **A massive increase of Chinese soft loans** and the **systematic subsidisation of its state-owned construction companies** in international competition, coincidentally at the same time when China closed its domestic construction market following its accession to WTO in 2001, thereby reducing the share of foreign contractors from 6% to below 1%.

5. **A distortion of international competition**, since the new competitors from emerging markets are not subjected to the **strict OECD regulations on environmental, social and ethical standards**, which have subsequently been transcribed into the national laws of OECD signatories.

New EU-Africa Strategy

EIC supports the new **"EU Strategy for Africa"** which has the objective to provide more and better development aid, to increase the speed of implementation and to focus aid on Africa. We welcome in particular the **"EU-African Partnership on Infrastructure"**, which promotes regional and continental interconnection at continental level, and the **"EU Infrastructure Trust Fund for Africa"**, which is an innovative financing instrument to significantly increase European funding for infrastructure projects in Africa.

For an effective implementation of the EU's ambitious infrastructure agenda in Africa, EIC deems it pertinent to take into consideration the conclusions agreed within the **Final Declaration of the first edition of the EU-Africa Business Forum** (*November 2006*) which are directed at the infrastructure sector:

- ✓ *"Generally, business considers that the **"project approach" for infrastructure** development should be maintained"*;
- ✓ *"The EC's infrastructure management capabilities* [should be] *reinforced with resources from the private sector and **robust project delivery mechanisms should be adopted**"*;
- ✓ *"The European Commission* [should] *form an **Africa Task Force** to address the strategic, policy, trade and infra challenges related to creating a level playing field with competitors from other regions. Key areas to focus on include: **export financing, export credit insurance, public procurement**"*;
- ✓ *"(Infrastructure) projects often overlook maintenance"*;
- ✓ *"To **pre-qualify** for Commission funding, companies should respect **environmental, social, financial standards within the EU acquis communautaire**"*.

Benefits of European private sector participation in infrastructure development in Africa

European infrastructure providers consider themselves as **reliable and competent partners for achieving the European Union's development goals in Africa**, since European companies are prepared to:

1. **Deliver quality infrastructure** over the entire **life-cycle of the project**, whilst Chinese contractors deliver sub-standard construction works which usually decay before their projected life-time;

2. **Employ and train the local workforce** in accordance with internationally recognised labour standards, whilst Chinese contractors "import" most of the labour from China and do seldom pay attention to international labour conventions;

3. **Co-operate with local contractors and suppliers** and **transfer technical know-how**, including their comprehensive experience on **Public-Private Partnerships**, whilst Chinese contractors have no interest in sharing their technology with local companies;

4. **Respect and protect the environment** through the recycling of waste and used materials and energy efficiency measures, whilst Chinese contractors sacrifice environmental concerns for price.

There are some good examples where the **presence of European infrastructure providers in Africa has lifted the local industry to a higher level**. More positive examples could certainly be realised since, when executing construction works overseas, European companies are no longer "exporting" a large amount of workforce, but are relying only on a very small number of key business personnel to manage the company/project in collaboration with local partners.

Basic prerequisites for European private sector participation in infrastructure development in Africa

European infrastructure providers have a world-wide reputation for delivering quality infrastructure and thus they prefer to participate in tenders which allow them to compete on their technical competence. They would recommend to the European donor community and the African partner countries to:

- **Design sizeable infrastructure projects** which would place European infrastructure providers in a position to become strongly engaged in Africa;

- **Prepare infrastructure tenders where the project budget indicates that quality of both design and execution is a priority**. It is of paramount importance that precise and state-of-the-art specifications and drawings are produced.

- **Establish coherence between the pre-qualification process for infrastructure projects and the EU's wider policy objectives** in the fields of protection of the environment, corporate social responsibility and business ethics, to the extent that only those bidders may participate in the competition that can demonstrate their ability to comply with the European Union's environmental, ethical and social policy objectives. The following information should be requested from bidders:

- *Quality assurance* and *environmental and social policy performance manuals*;
- *Know-how transfer statements* on the extent to which the local construction sector can participate in the contract, e.g. as Joint Venture partner, subcontractor or supplier;
- *Balance Sheet Audit according to U.S. GAAP or IFRS rules* in order to exclude companies benefiting directly or indirectly from state subsidies.

- **Introduce quality aspects into the tender procedure**, as the traditional rule for the evaluation of the contractor tenders, which is still the "lowest evaluated cost", has some critical side effects, such as:
  - In the *design phase*, the particular skills of experienced contractors cannot be taken into account, even though it is well-known that the biggest cost savings on a construction project are to be made at the outset of the project;
  - At *tender stage*, the conventional procurement method has an unfortunate bias towards the selection of the lowest evaluated tender, whilst, during the *construction phase*, it frequently turns out that the final completion costs have been seriously underestimated by the parties;

- **Utilise Conditions of Contract that reflect the latest industry standard** and provide for a **fair balance of risk**. The best way to ensure good contracting practice is the mandatory use of a internationally accepted standard contract form which, *inter alia*, provides for the enforcement of dispute settlement decisions through a Dispute Board and International Arbitration.

- **Proceed to alternative procurement methods** which offers the private sector the opportunity to **compete for both price and quality over the life-cycle of the procured service**, not simply for the lowest evaluated cost for the works. Such innovative methods provide a strong incentive for the private partner to perform well over time which offers Value for Money for the Contracting Authority and the European donor community.

DISCUSSION POINTS FOR EU-AFRICA FORUM IN ACCRA

For the second EU-Africa Business Forum in June 2007 in Accra (Ghana), EIC has identified three topics for discussion, namely:

1. Can European infrastructure providers bring **added value to Africa**? Can they help to leverage **additional private financial sources** for building Africa's infrastructure?

2. What are the tools available in order to build a **compromise between affordability** (price) **and sustainability** (quality) of infrastructure assets?

3. **How can African construction companies get better access to local or international credit facilities and better trained local employees** in order to partner with their European counterparts as Joint Venture partners or subcontractors?

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Introduction

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It has been widely acknowledged that the **improvement of infrastructure connections in Africa**, i.e. the transportation networks as well as the promotion of private sector participation in the delivery of electricity, water and sanitation services, is a precondition for achieving the ***Millennium Development Goals*** in Africa.[1] The European Commission estimates that between 2005 and 2015 Sub Sahara Africa needs to spend approximately 5% of its GDP on infrastructure investment and a further 4% on **operations and maintenance** – additional expenditure of **20 billion US$ per year**.[2] European infrastructure providers consider themselves as reliable and competent partners for achieving the European Union's development goals in Afica, since they are prepared to:

1. **Deliver quality infrastructure** over the entire **life-cycle of the project**;
2. **Employ and train the local workforce** in accordance with internationally recognised labour standards;
3. **Co-operate with local contractors and suppliers**;
4. **Transfer technical know-how**, including their comprehensive experience on **Public-Private Partnerships**;
5. **Respect and protect the environment** through the recycling of waste and used materials and energy efficiency measures.

[1] African Union / UN Economic Commission for Africa (UN ECA), *"Transport and the Millennium Development Goals in Africa"* (February 2005), page 1; UN ECA, *"The Millennium Development Goals in Africa: Progress and Challenges"* (August 2005), p. 18; World Bank Institute, *"Private Sector Involvement as a Vital Factor in Achieving the Millennium Development Goals"* (2005).
[2] Communication on *"Interconnecting Africa: the EU-Africa Partnership on Infrastructure"*, page 5, see http://ec.europa.eu/development/Geographical/europe-cares/africa/docs/1327_en.pdf.

Reasons for European disengagement from Africa

Despite the long tradition of engagement in Africa, it has become more difficult over the past fifteen years for European infrastructure providers to maintain a significant presence on the African continent, and in particular in the Sub Sahara region. Whilst European international contractors have successfully adapted their internationalisation strategies to the needs of the globalisation era and whilst they have more than doubled their international turnover since 1990 from then 53 billion US$ to some 120 billion US$, the same statistics reveal that only 5% of overseas works is carried out nowadays within Africa, compared to 15% in 1990. It seems, therefore, pertinent to recall the main reasons for the withdrawal of European companies:

1. **A sharp reduction by African governments and development partners of the share of resources allocated to infrastructure during the 1990s**.[3] It was – erroneously – anticipated by the international donor community that the private sector would step in and invest into privatised infrastructure service companies in developing countries. Subsequent experience showed, however, that the risks associated with privately financed infrastructure in the developing world were in many cases too high and thus the initial appetite of investors to engage in these types of projects decreased dramatically.

2. **A strategic realignment of the development policy of Multilateral and Bilateral Development Banks** which, despite shortcomings in partner countries' management systems, are shifting their financial support from project aid to **budget support** and the procurement rules from internationally harmonised Standard Bidding Documents to a rather diverse range of **Country Procurement Systems**.

3. **A growing importance of the financial markets as well as Corporate Governance requirements** motivated European infrastructure providers to focus increasingly on business profitability. This meant a concentration of activities on those foreign markets with a business-friendly legal framework and minimum political and economic risk as well as an evolution of many European contractors into construction-related service providers. Yet, European development agencies have hardly recognised this change of strategy, as they offer only a narrow market for privately operated infrastructure projects.

4. **A massive increase of Chinese soft loans** and the **systematic subsidisation of its state-owned construction companies** in international competition, coincidentally at the same time when China closed its domestic construction market following its accession to WTO in 2001, thereby reducing the share of foreign contractors from 6% to below 1%.[4]

5. **A distortion of international competition** provoked by the fact that the new competitors from emerging markets are not bound by the **strict OECD regulations on environmental, social and ethical standards** which have subsequently been transcribed into the national laws of OECD signatories. Obviously, such rules, if applied in Africa unilaterally to the OECD industry, place a crucial disadvantage on European infrastructure providers vis-à-vis its competitors from non-OECD countries.

[3] See Footnote 2, page 5.
[4] Study on the Future Opportunities and Challenges of EU-China Trade and Investment Relations (commissioned by DG TRADE), Study 9 on the Construction Sector, page 16.

New EU-Africa Strategy

European infrastructure providers remain, despite the described impediments, fully prepared to collaborate with the European Commission and the EU Member States, if framework conditions permit, in delivering sustainable infrastructure services to Africa. EIC, therefore, welcomes the new **"EU Strategy for Africa"**, adopted in December 2005, which has the objective to provide more and better development aid, to increase the speed of implementation and to focus aid on Africa. In support of this strategy, the European Commission has progressively launched a number of supporting initiatives of which three are of particular interest for EIC:

1. The **"EU-African Partnership on Infrastructure"** which promotes regional and continental interconnection at continental level;

2. The **"EU Infrastructure Trust Fund for Africa"** which is an innovative financing instrument to significantly increase European funding for infrastructure projects in Africa;

3. The **"EU-Africa Business Fora"** which brings together entrepreneurs and public and private investors from both Africa and Europe.

EIC has actively participated in the first edition of the EU-Africa Business Forum held on 16-17 November 2006 in Brussels, especially in the discussions of the so-called *"Interconnectivity Working Group"*. The European Commission is currently organising the second edition of the EU-Africa Business Forum which shall take place on 21-22 June 2007 in Accra (Ghana). One of the main objectives of the Accra Forum is to develop concrete action plans including time frames based on the recommendations and follow-up recommendations of the first edition. Hence, EIC would like to recall the following **conclusions agreed within the Final Declaration of the first edition of the EU-Africa Business Forum**:

- ✓ *"Generally, business considers that the **"project approach" for infrastructure** development should be maintained"*;

- ✓ *"The EC's infrastructure management capabilities* [should be] *reinforced with resources from the private sector and **robust project delivery mechanisms should be adopted**"*;

- ✓ *"The European Commission* [should] *form an **Africa Task Force** to address the strategic, policy, trade and infra challenges related to creating a level playing field with competitors from other regions. Key areas to focus on include: **export financing, export credit insurance, public procurement**"*;

- ✓ *"* [Infrastructure] *projects often overlook maintenance"*;

- ✓ *"To **pre-qualify** for Commission funding, companies should respect **environmental, social, financial standards within the EU acquis communautaire**"*.

Implementing the EU-Africa Partnership on Infrastructure

EIC observes that there are, in addition to the European Commission's communications on its "EU-Africa Strategy", at least **four other key documents** which present the background for further reflections on how the Commission can implement successfully the EU-Africa Partnership on Infrastructure.

1. EIC believes that the **Final Forum Declaration of the November 2006 EU-Africa Business Forum**, as quoted above, gives some important indications in which form and under which conditions the European private sector can make its contribution to the delivery of sustainable infrastructure services in Africa.

2. EIC acknowledges the principles stated in the **Paris Declaration on Aid Effectiveness of March 2005** ("Paris Declaration"), i.e. *Ownership*, *Harmonisation*, *Alignment*, *Results* and *Mutual Accountability*, and we would assume that in the light of the numerous critical voices which have pointed to the manifold infrastructure challenges in Africa, the fundamental objectives of *Quality* and *Sustainability* of aid delivery are also a true concern for the international donor community, and thus an inherent part of the five principles selected for the "Paris Declaration".

3. In order to avoid past mistakes and with a view to integrate the evaluation of past performance of European development aid into the future partnership strategy, EIC would like to recall as well the valuable analysis rendered by the **European Court of Auditors (ECA) in two Special Reports concerning the European Development Fund (EDF)** which were published in the years 2003 and 2005 and which, in our view, are relevant for the subject.

   The 2003 ECA Report concentrated on the execution of infrastructure works financed by the EDF and the Court then came to the conclusion that *"the European Union and the ACP States must improve the supervision of the implementation of works financed by the EDF and, in particular, must reduce the extent of divergences that were found between contracts and their actual implementation."* [5] The 2005 ECA Report concerned the EDF budget aid to ACP countries and the Court found that *"the Commission should… ensure that within each aid programme there is cohesion between the weaknesses recorded, the reforms that are to mitigate them, institutional support and follow-up tools. In addition, more attention must be given to matters relating to domestic revenue, including revenue from public undertakings, and corruption"*.[6]

Bearing in mind these analyses, EIC would like to present the private sector's perspective on the potential and the limits of putting into practice the key objectives of **Ownership, Quality, Accountability and Sustainability in the field of infrastructure services**.

[5] European Court of Auditors, Special Report No. 8/2003 concerning the execution of infrastructure work financed by the EDF, together with the Commission's replies, *cp. OJEC C 181*, page 4, see http://www.eca.europa.eu/audit_reports/special_reports/docs/2003/rs08_03en.pdf.
[6] European Court of Auditors, Special Report No. 2/2005 concerning EDF budget aid to ACP countries: the Commission's management of public finance reform aspect, together with the Commission's reply, *cp. OJEC C 249*, para. 84, see http://www.eca.eu/audit_reports/special_reports/docs/2005/rs02_05_en.pdf.

COUNTRY OWNERSHIP

In the context of the EU-Africa Partnership for Infrastructure, the Commission calls for renewed **African ownership and leadership** in the process of setting priorities, making progress on regional integration, sound institutional and economic governance and transparent procurement.[7] The OECD recommends in this context that partner countries develop comprehensive infrastructure strategies, linked to other economic and social sectors and plans. Developing such strategies requires responsive government entities, clear regulations and participation by accountable stakeholders.[8]

Due to the complexity of infrastructure projects, e.g. in road transport, African governments and European bilateral donors are limiting themselves today mostly to the financing and construction of labour-intensive rural roads. Whilst, admittedly, direct income and employment effects can be achieved through labour-intensive construction, compared with **capital-intensive construction by experienced international contractors** this means longer implementation periods and lower production efficiency. Bearing in mind that the construction quality is generally poorer, the costs per kilometre of road of labour-intensive works usually exceed those of a capital-intensive construction process. Furthermore, impact analyses have shown that such direct income effects frequently remain temporary.[9]

The economic and social progress in Asia over the last 50 years shows, however, that coherent and well maintained infrastructure networks have made a significant contribution to the development of the private sector and the employment of the local population. Therefore, EIC would recommend to African partner countries and European donors to **design sizeable infrastructure projects** which would provide European infrastructure providers with a possibility to become again engaged in Africa and to **bring added value to the local construction sector**, particularly with a view to the policy goal that operation & maintenance responsibility be transferred progressively to the (local) private sector, for which there needs to be a sufficiently large number of medium-sized construction firms.[10]

Still, the World Bank recently noted that Africa is widely recognised as a high-cost, high-risk place to do business. Africa-owned firms are largely constrained by limited access to finance, a restrictive business environment with strong incentives for informality, and poor management and technical capacity.[11] There are good examples, however, where the **presence of European infrastructure providers in Africa has lifted the local industry to a higher level**. EIC believes that many more positive examples could be realised since nowadays, when executing construction works overseas, European companies are no longer "exporting" a large amount of workforce to distant sites, but are relying only on a very small number of key business personnel to manage the company/project in collaboration with local partners.

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[7] See Footnote 2, page 6.

[8] OECD Development Co-operation Directorate, *"Guiding Principles on Using Infrastructure to Reduce Poverty"*, (March 2006), page 6; *cp*. www.oecd.org/dataoecd/43/45/36427725.pdf.

[9] KfW Development Bank, Ninth Evaluation Report (2004/2005) on Projects and Programmes in Developing Countries (November 2006), page 30.

[10] See Footnote 9, page 32.

[11] World Bank, *„Accelerating Development Outcomes in Africa – Progress and Change in the Africa Action Plan"* (April 2007), para. 43.

QUALITY

The World Bank has found in a recent update to the *"Africa Action Plan"* that **transport costs in Africa are the highest in the world, because of the lack and substandard quality of transport infrastructure**.[12] As a consequence, reducing the cost and **improving the quality of transport services is central to the transport-related part of the EU development policy**.[13] A key element in the delivery of quality infrastructure is the procurement system. In this context, the above-mentioned 2003 ECA Report notes that, *"shortcomings and errors in the design and implementation studies were the source of many of the implementation problems found, and the absence of any quality control of these studies meant that too many contracts were based on partly incorrect or unrealistic terms and conditions"* in relation to infrastructure works financed by the EDF. [14]

European infrastructure providers have a world-wide reputation for delivering quality infrastructure and, taking into due consideration the impediments referred to before, they prefer **to participate in infrastructure tenders** in which they can compete on their technical competence, i.e. on quality.

Planning and Design phases: Realistic project budgets

European infrastructure providers are deterred from participating in tenders where the project budget indicates that quality of design and execution are not a priority. In our experience, the root of many problems in infrastructure projects is sub-standard documents which in turn result from under-funding at the design stage. There is also little evidence that partner countries do budget adequately for broader development objectives when setting the estimates of project costs.[15] Since omissions and ambiguities in the tender documents will materialise at a later stage, it is of paramount importance that, once the project has been identified in consultation with all stakeholders, **precise and state-of-the-art specifications and drawings are produced**. Regrettably, EIC is aware of cases where (bilateral) donors decided to cancel the entire tender procedure in the light of bid prices exceeding the agency's project budget and, instead of re-examining the design studies, disbursed the development funds subsequently through the budget aid modality.[16] To give incentives for change of such habits, the Court of Auditors has proposed that *"quality controls should be increased for studies and consultants should be held financially liable for any professional negligence on their part"*.[17]

Tender phase: Stringent pre-qualification

European infrastructure providers are capable and willing to make a positive contribution to achieving the Millennium Development Goals in Africa; yet, they feel that the current tender procedures in donor-funded projects normally do not appreciate such readiness. In order to re-establish a **level playing-field**, EIC suggests that the pre-qualification process

[12] See Footnote 11, para. 65.
[13] See Footnote 2, pages 7 and 16.
[14] See Footnote 2, page 4.
[15] Engineers Against Poverty / Institution of Civil Engineers, *"Modifying infrastructure procurement to enhance social development"* (November 2006), page 19; *cp*. http://www.engineersagainstpoverty.org.
[16] e.g. Chalinze-Segera-Tanga Road (Tanzania).
[17] See Footnote 5, page 16 (para. 38).

should be coherent with the European Union's wider policy objectives in the fields of protection of the environment, corporate social responsibility and business ethics, to the extent that only those bidders may participate in the competition that can demonstrate their **ability to comply with the European Union's environmental, ethical and social policy objectives**. Therefore, in addition to the "normal" statements, the following information should be requested from the bidders and be strictly scrutinised by the Contracting Authority and the Consulting Engineer:

- *Quality assurance* and *environmental and social policy performance manuals*;
- *Know-how transfer statements* on the extent to which the local construction industry can participate in the contract as Joint Venture partner, subcontractor or supplier;
- *Balance Sheet Audit according to U.S. GAAP or IFRS rules* in order to exclude companies benefiting directly or indirectly from state subsidies.

Project award phase: Quality-Based Selection

European infrastructure providers believe that the traditional rule for the evaluation of the construction tenders, which is still the "lowest evaluated cost", should be enhanced by the introduction of quality aspects into tender procedure. Whereas the EU's Procurement Guidelines for *Consultants* and other *Services* explicitly prescribe the evaluation of the consultant tenders in two separate stages – first the quality and then the cost – bidders for construction works still have the option of submitting an aggressive bid with a very low price and trying to recoup the remainder later, either from the Contracting Authority or through hidden subsidies.[18] To avoid such dubious practices, EIC would like to remind donors and Contracting Authorities of the various technical tools available to introduce quality aspects into the selection phase, such as broadening the scope of the award criteria from financial only to technical and environmental elements or asking bidders to submit Alternative Proposals with their tenders or evaluating the financial aspect only once the technical merits of the tender have been assessed.

Execution phase: Fair Contract Conditions

European infrastructure providers working abroad would expect in donor-financed infrastructure projects that the Conditions of Contract reflect the latest industry standard and provide for a fair balance of risk. The best way to ensure good contracting practice is the mandatory use of a standard contract form which, *inter alia*, provides for the enforcement of dispute settlement decisions through a Dispute Board and International Arbitration. The Multilateral Development Banks have recently decided to harmonise their standard contract conditions for major works on the basis of the FIDIC standard and to use the so-called ***"MDB Harmonised Edition of the FIDIC Conditions of Contract for Construction"***. Given the reputation that the 1999 FIDIC standard forms of contract for Construction and for Plant and Design-Build have on the international market, and since these documents were used successfully by the Commission already in connection with ISPA projects, EIC believes that the time has now come for the European Commission to eventually update its General Contract Conditions and thus to respond positively to the Recommendation No. 6 of the 2003 ECA Report that *"the general conditions relating to the implementation of works contracts… should be re-examined in the light of the experience acquired since* [1990].*"*[19] Such a decision would certainly raise the interest of the European companies in EDF-financed infrastructure projects.

[18] There is anecdotal evidence that the bid prices of Chinese competitors in Africa are generally 40% below the European bid prices, as Chinese companies seem to calculate only the local costs in the country,i.e. manhours, material, subcontractors, equipment, gasoil of European competitors.
[19] See Footnote 5, page 17 (para. 43).

ACCOUNTABILITY

In order to provide the partner Countries with a better sense of **ownership**, the international donor community has vowed in the "Paris Declaration" to *"**use country systems and procedures** to the maximum extent possible"* (para. 21). The European Union has set itself the target in the "European Consensus on Development" of November 2005 to progressively increase the **budget support aid modality**, where circumstances do permit.[20]

EIC supports the long-term goal to increase transparency and accountability in developing countries' procedures; however, the introduction of such decentralisation policies in institutionally weak management systems may have the opposite effect and thus **expose European taxpayers' money to the usually high risks affecting those procedures**.[21] The Court's concerns are legitimate and have been addressed by the international donor community: For instance, the "Paris Declaration" clarifies that *"where corruption exists, it inhibits donors from relying on partner country systems"* (para. 4) and it states also that *"a major concern for partner countries and donors is to enhance mutual accountability and transparency in the use of development resources"* (para. 47).

In the field of consultancy services, two recent World Bank studies on Effectiveness and Professional Integrity come both to the conclusion that the Bank should strive at amplifying its aspirations and standards for Quality, Integrity and Sustainability in the procurement for infrastructure works rather than leaving these crucial responsibilities to its borrowers. The studies found that an obvious effect of a flawed procurement system is the absence of experienced companies.[22] EIC concurs with the analyses of the two World Bank studies and relies on the European Commission's finding that *"**donor managed projects might be a preferable aid mechanism** where transaction costs are lower for the donor than for the partner government. This might be the case for **large international*** [infrastructure] ***tenders** where the partner government does not possess the necessary capacity to effectively manage the overall contracting process"*.[23] EIC is thus concerned that an increased use of budget aid and Country Procurement Systems lead to a watering down of relevant international standards safeguarded presently by the Standard Bidding Documents of the multilateral and bilateral donor agencies.

Last but not least, the Commission should be aware that EDF funds provided directly as budgetary aid under a sector wide programme may be utilised as the national co-financing portion to **non-European tied-aid type of soft loans without eligibility for European infrastructure providers**.[24] EIC very much doubts that European taxpayer's money should be abused for such co-financing schemes and asks the Commission to take the necessary precautions.

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[20] European Council Doc. 14820/05, OJEC C46/1, para. 26.
[21] *cp.* Footnote 6, paras. 12 and 29..
[22] Casartelli/Wolfstetter, *World Bank Policy on the Selection and Employment of Consultants: Study of its Effectiveness* (2007); Schwenke: *Promoting Integrity and Constraining Corruption in the Selection and Employment of Consultants* (2007).
[23] EuropeAid Cooperation Office, *"Aid Delivery Methods-Volume 1: Project Cycle Management Guidelines"* (March 2004), page 14.
[24] For instance EDF Commitment for Ethiopia's Sector Policy Support Programme in support of Ethiopia's Roads Sector Development Programme (RSDP) and the subsequent soft loans in connection with the Azezo-Gente road project, e.g. Afrique Projets, Numéro 186, 09 Octobre 2006.

SUSTAINABILITY

One of the key aspects of infrastructure asset sustainability is that **adequate arrangements must be made at the planning stage to finance operation and maintenance**. Traditionally, clients and donors have mostly failed to consider the life-cycle costs of an asset. This has led to infrastructure such as roads deteriorating to such an extent that large-scale costly rehabilitation works are required.[25] The European Commission estimates that deferred maintenance has resulted in the loss of one third of the capital invested in the Sub Sahara Africa road network.[26]

The Commission's analysis matches the growing consensus in the international development community that the **key challenge** in connection with infrastructure works is the **necessity to maintain, rehabilitate and operate the assets** following the construction phase. The World Bank is, therefore, examining the possibility of alternative forms of procurement and it has commissioned in 2003 a study which came to the conclusion that *"there are a number of very significant benefits to be gained by all concerned when using* ***Performance-Based Procurement*** *of infrastructure type projects. For large, complex projects, the benefits would appear to far outweigh any negative aspects."* [27] For the transport sector in particular, the Bank has issued very recently Sample Bidding Documents for Procurement of Works and Services under "Output-and Performance-Based Road Contracts" (OPRC) to provide its clients with an alternative to the traditional procurement methods. The documents focus on Performance based Management and Maintenance of Roads, but are also suitable for the procurement of works and services under **longer-term "Design-Build-Operate-Maintain (DBOM)" contracts**.[28]

EIC very much welcomes the fact that the international donors eventually are trying to respond to the challenge of infrastructure maintenance and operation. We have tried to explain in great detail[29] that the procurement of large and complex infrastructure projects poses a big challenge to Contracting Authorities around the globe because of the **many interfaces connected with the traditional design-bid-build approach**. This traditional approach, which is globally still the usual way of procurement, has some critical side effects:

- In the *design phase*, the particular experience and skills of experienced contractors cannot be taken into account, even though it is well-known that the **biggest cost savings on a construction project are to be made at the outset of the project**;

- At *tender stage*, the conventional procurement method has an unfortunate bias towards the selection of the lowest evaluated tender, whilst, during the *construction phase*, it frequently turns out that the final completion costs have been seriously underestimated by the parties. The practical consequence is that there is a **long proved track-record of conventionally procured construction projects, particularly in the infrastructure sector, delivered delayed and over budget**;

[25] See Footnote 16, page 18; *cp*. Gunter Zietlow, *"Financing and Management of Roads in Sub-Saharan Africa – A HopelessCase?"*
http://www.sutp.org/index.php?option=com_content&task=view&id=424&Itemid=40&lang=ef
[26] See Footnote 2, page 15.
[27] *"Study on Performance-Based Procurement of IFI and donor-funded large, complex projects"*, dated 29 March 2004, commissioned by the World Bank's Procurement Policy Department
[28] *cp.* http://www.worldbank.org/procurement - enter "OPRC"
[29] EIC Blue Book on Sustainble Procurement, *cp.* http://www.eicontractors.de/seiten/focus/contract.php

- Even if capital costs are originally well spent, the traditional procurement method does not provide for a mechanism to draw on the **private sector's management expertise**, including control of costs, during the *operation and maintenance phase*.

Moreover, maintenance problems can often be traced back to **institutional deficiencies**, e.g. the division of public funding into separate capital and revenue accounts. The procured assets are not operated and maintained in a cost-efficient way because conventional public sector budget planning takes place on a yearly basis, at maximum on a 3-year term, a period which is too short to optimise construction and operation requirements. Another frequent experience, not only in developing countries, shows that **maintenance is frequently the first target for spending cuts under tightening public budgets** even if delaying preventive maintenance results in much higher eventual overall costs over the project's life-cycle. Ultimately, such negligence leads to a significant or complete loss of the residual value of the asset.

Against this background, EIC considers the DBOM approach as an innovative mechanism to **integrate the key drivers of Value for Money**, i.e. *output-based specification*, *risk transfer*, *life-cycle costing*, *performance measurement and incentives*, *competition* and *private sector management skills*, into all phases of the project cycle. The DBOM concept offers an **alternative procurement method** which can help to overcome the described defects by shifting the long-term planning risk for an infrastructure project to the private sector which, given the competitive tender situation, has a commercial interest in optimising construction and operation management over the duration of the contract. The concept differs from the traditional procurement route in that it invites the private sector to compete for both price and quality over the life-cycle of the procured service, not simply for the lowest evaluated cost for the works. It provides a strong incentive for the private partner to perform well over time which, of course, offers substantial advantages for the Contracting Authority (Value for Money):

- **Up-front and full cost transparency and security** in terms of capital investment as well as subsequent costs for operation and maintenance;

- **Substantial risk transfer to the private sector**, including all interface risks between planning, design, construction and operation of the project;

- **Annuity payments dependent on the performance quality of the service itself**, not merely the quality of the works required for the service.

European infrastructure providers are very experienced in DBOM type of contracts and would certainly be interested in these types of projects in Africa. Whilst the advantages for the donors and the Contracting Authority have been described above, it should also be underlined that **the local private sector will benefit from the implementation of the DBMO concept**, since a significant part of the physical works and particularly the O&M phase will be executed through local small and medium-sized companies (SMEs). Hence, the DBMO approach is both an opportunity for innovative local SMEs to expand their skills into the design and operation phase under the guidance of an experienced international contractor.

The European Union would be particularly well suited to finance such long-term contracts in Africa, since it can combine grant elements from the EDF with loans elements from the EU Member States. A third source of finance, the European Investment Bank, has been recently connected through the **"EU Infrastructure Trust Fund for Africa"**.

OUTLOOK

EIC would like to reiterate that European infrastructure providers consider themselves as vital partners for future infrastructure development in Africa. They are willing to bring to the continent their experience, skills and willingness to partner with all actors designated to improve Africa's infrastructure networks, in particular with the African private sector that is active in the field of infrastructure. For the second EU-Africa Business Forum in June 2007 in Accra (Ghana), EIC has identified three topics for discussion, namely:

1. Can European infrastructure providers bring **added value to Africa**? Can they help to leverage **additional private financial sources** for building Africa's infrastructure?

2. What are the tools available in order to build a **compromise between affordability** (price) **and sustainability** (quality) of infrastructure assets?

3. **How can African construction companies get better access to local or international credit facilities and better trained local employees** in order to partner with their European counterparts as Joint Venture partners or subcontractors?

Within the framework of the 10th European Development Fund, a total amount of 5.6 billion € has been allocated for the period 2008-2013 for the development of the EU-Africa Partnership for Infrastructure. The EDF financing will be supported by additional funds from the "EU Infrastructure Trust Fund for Africa" and bilateral programmes of EU member states may also contribute to the partnership. Against this positive background, there is reason for a new optimism for a sustainable infrastructure development in Africa.